BEFORE THE PUBLIC UTILITIES COMMISSION

OF THE STATE OF HAWAII

ORIGINAL

In the Matter of the Application of)
HAWAIIAN ELECTRIC COMPANY, INC.) DOCKET NO. 2008-0083
For Approval of Rate Increases and)
Revised Rate Schedules and Rules.)

TRANSCRIPT OF PROCEEDINGS

VOLUME III

Public Utilities Commission hearing held on Wednesday, October 28, 2009, commencing at 9 a.m., at 465 South King Street, Honolulu, Hawaii, pursuant to Notice.

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E X H I B I T S

P R O C E E D I N G S

CHAIRMAN CALIBOSO: Good morning, everyone.

I'd like to call this proceeding back to order.

For the record, my name is Carlito Caliboso, Chairman of the Public Utilities Commission, joined by Commissioner John Cole and Commissioner Leslie Kondo. We have a consultant Scott Hempling.

The parties appearances for the record, please.

MR. ALM: Good morning, Mr. Chairman, Mr. Cole, Mr. Kondo, and Mr. Hempling.

Thomas Williams appearing on behalf of Hawaiian Electric Company.

MR. ITOMURA: Good morning, Chair Caliboso, Commissioner Cole, Commissioner Kondo, Mr. Hempling.

John Itomura on behalf of the Consumer Advocate. With me is Cat Awakuni and Dean Nishina from the Consumer Advocacy.

CHAIRMAN CALIBOSO: Good morning.

MR. MCCORMICK: Good morning, Chairman and Commissioners.

Representing the Department of Defense will be James McCormick and Dr. Kay Davoodi.

CHAIRMAN CALIBOSO: Thank you.

Good morning, everyone.

Are there any procedural matters we need to take care of before we begin?

Any hearing exhibits?

MR. WILLIAMS: I believe we were filing some hearing exhibits on the sales issues. We had previously circulated them to the parties.

CHAIRMAN CALIBOSO: Are you ready?

MR. ALM: I don't know.

CHAIRMAN CALIBOSO: We can do it later.

MR. WILLIAMS: Okay. Because that's actually for the next panel.

CHAIRMAN CALIBOSO: All right. Thank you.

With that, we'll start with -- continue with the CT-1 panel.

Mr. Hempling?

MR. HEMPLING: Thank you, Mr. Chairman.

I'd like to address some questions concerning the interaction between the ECAC, that's E-C-A-C, and the CT-1 unit.

Mr. Brosch, did you work on this issue with the Consumer Advocate?

MR. BROSCH: Depending on the nature of your questions, I expect Mr. Herz will be --

MR. HEMPLING: Okay.

MR. BROSCH: -- the best in responding.

MR. HEMPLING: Could everybody turn in the

Settlement Exhibit, the Exhibit 1, page 15 of 90.

Are you there, sir?

MR. HERZ: Yes, I am.

MR. HEMPLING: Did you cover this area in terms of dealing with the Settlement?

MR. HERZ: Yes, I did.

MR. HEMPLING: Okay. What I want to do for the Commission is make sure we understand how different fuel uses by the CT-1 unit will effect the assumptions underlying the Settlement Agreement's treatment of the energy cost adjustment factor. Okay?

MR. HERZ: Yes.

MR. HEMPLING: That's the subject here.

Are you familiar with that subject?

MR. HERZ: Yes, I am?

MR. HEMPLING: All right. First, Mr. Herz, how would the fuel choice of CT-1 affect it heat rate?

Do you know?

MR. HERZ: The heat rate is not influenced -- CT-1 is not influenced so much by fuel choice as it is by how the unit is dispatched in the system.

MR. HEMPLING: What type of fuel won't make a difference?

MR. HERZ: It does from the standpoint that bio -- if the fuel is higher cost, the unit is dispatched less; and, as a result, the heat rate will then be less.

MR. HEMPLING: Okay. So can you give us a sense of the differential that would occur as between biofuel and other fuel?

MR. HERZ: Yes, the page that you had referenced, if you'll notice near the bottom, there's a heat rate for bio-diesel.

MR. HEMPLING: Yeah, and before we get mixed up, I want to make sure that you mean to be on page 15 and not on page 16, where the numbers are slightly different.

One is the Company proposal and the other is the Settlement result.

Which one do you want to be talking about?

MR. HERZ: We could refer to either one.

MR. HEMPLING: Well, which one?

MR. HERZ: Well, let's start with page 15, for example.

MR. HEMPLING: Okay. So you're now referring to the Company's proposal.

Go ahead.

MR. HERZ: You'll see that the heat rate for bio-diesel is .022909, and it's not shown separately here for CT-1 for its diesel operation; but, if you were to look at CT-1 under diesel fuel, you'd see that the heat rate is less than the amount that's shown for bio-diesel in CT-1.

MR. HEMPLING: Okay. What's the difference?

MR. HERZ: The quantity, is that -- is that your question --

MR. HEMPLING: Yes.

MR. HERZ: -- or qualitatively?

MR. HEMPLING: Quantity.

MR. HERZ: One moment, please, while I look that up.

MR. HEMPLING: Is this your area too, Mr. Sakuda?

MR. SAKUDA: Yes, it is.

MR. HEMPLING: Good morning.

MR. SAKUDA: Good morning.

MR. HEMPLING: Is he doing okay over there?
He's on top of this so far.

MR. SAKUDA: Yes --

MR. HEMPLING: Okay.

MR. SAKUDA: -- I follow.

MR. HEMPLING: Okay. Do you agree we've been already saying so far that the heat rate is going to be more favorable with -- less favorable with biofuel than with diesel?

MR. SAKUDA: Yes, if the fuel price for bio-diesel fuel is higher that that for diesel it maybe dispatched more, but it depends on what the system mode is.

MR. HEMPLING: Anytime you have an answer with the word "may," it can include may not, which means there's no answer.

MR. SAKUDA: It may or may not because it may still operate at minimum load.

MR. HEMPLING: I see. Okay, thank you.

Mr. Herz?

MR. HERZ: What I'm saying is that for the test year is that, under our dispatch analysis, the CT heat rate under diesel was actually higher than bio-diesel; and, I'd have to dig deeper, but I suspect the reason is, is that when the CT unit under diesel is being operated, it's being dispatched economically against the system and can be used primarily in a peaking mode; whereas, with the bio-diesel, during the test period, the bio-diesel was being used as part of the testing of the unit performance and emissions with the bio-diesel; and, so I suspect that we've modeled it in differently than being economically dispatched against the system.

MR. HEMPLING: When you say, "We've modeled it in," are you referring to for purposes of the settlement or for the purposes of your testimony?

For what purposes did you do this modeling?

MR. HERZ: The modeling, for the purpose of my testimony, was the same as for the purpose of the Settlement.

MR. HEMPLING: Maybe I can get to my bottomline if you can help me work backwards more efficiently than I'm doing it here.

The Settlement number for the energy cost adjustment factor is what?

MR. HERZ: It's -- for bio-diesel, it's .016762 on page 16.

MR. HEMPLING: No, I think, I either mis-asked or you mis-answered.

Isn't the energy cost adjustment factor 0.152 cents per kWh?

MR. HERZ: I'm sorry. Yes.

MR. HEMPLING: Say it again, please.

MR. HERZ: Yes.

MR. HEMPLING: Yes, why?

MR. HERZ: Yes the resulting the ECAF factor under current rates is 0.152 cents per kWh.

MR. HEMPLING: And that's a composite of the heat rates associated with the various fuels. Right?

MR. HERZ: Yes.

MR. HEMPLING: Okay. So what did you assume for Settlement purposes for the energy cost adjustment factor?

MR. HERZ: Zero in that the energy cost adjustment factor basis and heat rates would be modified so as to result in a zero ECAF --

MR. HEMPLING: Okay. So --

MR. HERZ: -- the proposed rates, yes.

MR. HEMPLING: I'm sorry.

MR. HERZ: Yes, the proposed rates.

MR. HEMPLING: All right. So the heat rates that are listed at the Settlement heat rates on page 16, what do those heat rates assume about the operation of a CT-1 unit that it would be operating with biofuel or with conventional fuel?

MR. HERZ: It assumed that CT-1 would be operating on diesel for the months August through November. For the period, December 1st through December 14th, the unit would be operating on bio-diesel; and, then for the remaining of the month of December in 2009, the unit would be down for maintenance and inspections.

MR. HEMPLING: So you're just talking about 2009?

MR. HERZ: Yes.

MR. HEMPLING: Well, help the Commission understand under what circumstances going forward during the year in which the rates were in effect would the Settlement assumptions lead to overrecovery or underrecovery of fuel costs.

MR. HERZ: I don't believe that on a good-forward basis there would be an over- or underrecovery of fuel costs if the modifications to the ECAC being proposed as part of the Settlement or adopted; and, included in the modifications is that a separate heat rate will be established by fuel type; and, of course, one of those fuel types would be biofuel.

And then to the extent that biofuel is actually used in CT-1 on a going-forward basis, then those costs would be passed through the ECAC using the biofuel of heat rate.

On the other hand, if the unit operates on diesel, those field costs would be passed through using the diesel heat rate. So regardless of what happens on a going-forward basis, the ECAC with the modification and the addition of the biofuel diesel heat rate or -- excuse me -- the biofuel heat rate would result in a pass-through of cost matching the actual operations.

MR. HEMPLING: And the dispatch practices with respect to the unit would not effect then the possibility of overrecovery or underrecovery?

MR. HERZ: To the extent that the Company operated these units in a manner different than what was assumed in the test year and the heat rate was different then, yes, there would be the possibility of an over- or underrecovery of fuel costs. That is one of the consequences of having a fixed heat rate in the ECAC calculation.

MR. HEMPLING: Well, that's what I'm trying to understand.

What is the likelihood that the dispatch of the unit will vary from what's assumed in the test year?

Do you know?

MR. HERZ: I don't -- I don't know. If some of the unit is continued to be operating on an economic dispatch basis, the biofuel will be the higher fuel, higher priced fuel used in the -- it's most likely to be a higher priced fuel used in the Company's generating units and, therefore, would be one of the last units dispatched.

So to the extent that there is a difference in the heat rates, the significance may not be very large if the unit isn't used very much and, therefore, there isn't much kilowatt hours or fuel consumption related to the operation of CT-1.

MR. HEMPLING: So are we looking at a small enough number of dollars that we should just not focus on this in terms of the variation in costs pass-through as a result of the variation in the heat rates as a result of the variation in dispatch practices?

MR. HERZ: For ratemaking purposes in this proceeding, I think it is a nonfactor; and, I don't know if "ignored" is the right word, but it's not significant, in my mind, to affect the net revenue requirements that need to be generated by rates or the setting of rates in this proceeding.

MR. HEMPLING: Anything to add to this conversation, Mr. Sakuda?

Don't complicate it, if you like the way it's gone.

MR. SAKUDA: I agree that it is insignificant; and, just to put it in context, the total biofuel expense in the final settlement was $179,000 compared to a total fuel oil expense of $431.2 million, which is only .018 percent of total fuel oil expense; so, it is insignificant.

But I do want to address Mr. Herz's comment about having heat rates assigned for the ECAC based on heat rates assigned to the different fuels. We currently do it based on a composite weighted heat rate; and, I don't see a reason to move away from what we currently do.

MR. WILLIAMS: Oh, I'm sorry. Mr. Hee is the ECAC witness.

MR. SAKUDA: Okay. I'm sorry, I overstepped my bounds.

(Laughter.)

MR. SAKUDA: Mr. Hee is the ECAC witness.

MR. HEMPLING: Well, did you overstep it accurate or inaccurately?

MR. SAKUDA: Inaccurately.

MR. HEMPLING: Inaccurately?

MR. SAKUDA: It should be -- yes -- by fuel type as shown on page 16 of the Settlement.

MR. HEMPLING: Restate your answer so I know which one to believe.

(Laughter.)

MR. SAKUDA: We are proposing to provide or calculate the ECAC according to the different fuel types, which includes the low sulfur fuel oil diesel, bio-diesel and there is a weighted average at the bottom.

MR. HEMPLING: What is it weighted by?

MR. SAKUDA: It's weighted by consumption.

MR. HEMPLING: All right. Anything else, Mr. Sakuda?

Stay out while you've still ahead.

(Laughter.)

MR. SAKUDA: Yes, I'm done.

MR. HEMPLING: Okay. Thank you. Okay. Let's go to -- no, excuse me one second.

COMMISSIONER KONDO: I have some CT-1 questions. I think they're financial in nature, so I don't if that's Ms. Nanbu or Ms. Sekimura, but I want to ask some questions about impact on CT-1, financial.

Ms. Sekimura, all set?

MS. SEKIMURA: Yes.

MR. WILLIAMS: Mr. Chairman, just a scheduling question.

Our we expecting the next panel soon?

And I need to call over and have them come over here.

(Whereupon, Mr. Hempling briefly confers with the Commission.)

CHAIRMAN CALIBOSO: Probably, in most, another half an hour, maybe a little less.

MR. WILLIAMS: Thank you.

COMMISSIONER KONDO: Good morning.

I want to make it absolutely clear in my own mind, and I apologize if we've gone over this yesterday, if I don't use the right terms; but, I'm just trying to get a good understanding for my own self.

But I understood from yesterday's discussion that CT-1 was booked to plant and service August 3rd, or some date similar to August 3rd or around August 3rd; is that correct?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: Okay. Does that mean or I understood that to mean that, at that point, the Company stops collecting AFDUC; is that correct?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: Is there any money or any what I'm going to call interest to the Company or return to the Company is recovering on CT-1 at present?

MS. SEKIMURA: No. At the time, we stopped AFDUC, we're not collecting on those carrying costs.

COMMISSIONER KONDO: What is the total amount that was booked to plant and service?

Is there a dollar figure that's billed to plant and service on your book?

MS. SEKIMURA: Yes, there is a dollar amount.

COMMISSIONER KONDO: And what is that dollar amount?

MS. SEKIMURA: That was booked at that time, I would need to refer to Mr. Isler.

MR. WILLIAMS: Just one clarifying question, when we talk about CT-1, are we talking about the whole project or we're just talking about the generating component, because I think in our IR response we indicated there were two components, at least, that had not yet been completed as of that date?

COMMISSIONER KONDO: Okay. And thank you. I want to ask some questions about that as well.

But what is the amount that's been booked to plant and service?

MS. SEKIMURA: The amount is approximately 176 million.

COMMISSIONER KONDO: And, from Mr. Williams' comment, I take it that does not include the two components of the project, the black start generators and the water treatment system that were specifically referenced in the IR response; is that correct?

MS. SEKIMURA: That's correct. Right, but the 176 does not include the costs for the black start, which was closed on October 15th.

COMMISSIONER KONDO: When you mean -- when you say "closed," does that mean that the black star generator --

MS. SEKIMURA: I'm trying --

COMMISSIONER KONDO: -- was booked to plant and service --

MS. SEKIMURA: Plant and service.

COMMISSIONER KONDO: I'm sorry, we shouldn't talk over each other, all right, for him.

But does that mean that it was booked to plant and service on October 15th?

MS. SEKIMURA: Yes.

COMMISSIONER KONDO: And what was the amount that was booked to plant and service for the black star generator?

MS. SEKIMURA: The amount that was booked was about 6.5 million.

COMMISSIONER KONDO: For the black star --

MS. SEKIMURA: I'm sorry --

COMMISSIONER KONDO: -- generator --

MS. SEKIMURA: I'm sorry.

COMMISSIONER KONDO: -- or the water treatment system?

MS. SEKIMURA: I'm sorry. For the black start, it was 3 million.

COMMISSIONER KONDO: And the water treatment system still is under construction for the Company?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: So what I've learned in this process is that currently you're collecting AFDUC on that amount with relating to the water treatment system?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: What is the difference between the estimated costs of the project, which I understood to be $193,100,000 and the numbers that we've talked about so far, the amount that was booked to plant and service, 176; black star generator, 3 million, and I understand the estimate for the water treatment system was 6.5 million?

Can you explain where that difference is, what's missing there, 193 and 176 plus 3, plus 6.5?

MS. SEKIMURA: I believe there are some additional costs associated with the CT-1, not including the water treatment and black start, that are still needing to be incurred.

COMMISSIONER KONDO: Do you know what those would be?

MS. SEKIMURA: Could I please defer that to Mr. Isler?

MR. ISLER: Could you repeat the question, please?

COMMISSIONER KONDO: Sure.

I was asking Ms. Sekimura about what the difference was between 193,100,000, which I understood to be the estimate of the total costs of the CT-1 project; and, the number that was booked to plant and service, which was 176 million, the black start generator, 3 million, and the water treatment system 6.5 million. They don't add up to 193,100,000.

So I was curious as to what made up the difference?

MR. ISLER: Okay. As of August 3rd, there were many different components that had been booked to plant and service. It's not just the generating facility. We have the transmission line and the substations and other parts.

As of August 3rd, I'm not sure what the exact number that was booked to plant, but it did not include any of the estimated costs for the black start diesel generators or on the water treatment, which totals around $9.5 million. It also did not include any expenditures for the rest of the components that we haven't paid for yet.

There have been certain -- sometimes services are rendered but invoices are paid later and sometimes there are still some additional work that needs to be done, even though the plant is in a position where it can be placed in service.

COMMISSIONER KONDO: And of those types of things that you described, that totals about $8 million?

MR. ISLER: Let me do the math.

COMMISSIONER KONDO: I mean, is it in that magnitude?

Are you talking about costs?

MR. ISLER: Yes. The difference, it's actually probably a little bit more than that. The 176 million that was told to you was actually what the total costs of the project was as of, you know, sometime in September; and, that did include some costs for water treatment and for black start that's been expended so far.

So we're not quite comparing apples to apples here. The total amount -- I'm not sure what the total amount book to plant was on August 3rd, but it was likely -- it was definitely less than 176. It was probably in the range of 155 to 160 million. I'm not exactly sure.

COMMISSIONER KONDO: I thought Ms. Sekimura's testimony was 176 was billed to plant and service on August 3rd.

So what are you saying?

I didn't understand the comment about 150 (sic) million. And if this is not your area, I'm okay with you passing.

MR. ISLER: No, no. I think the confusion comes in to -- as of September 28th, and based on the costs report that we had put in, we had expended a total of $176 million for all the different components, including ones that had not been placed in service yet; so, the amount that had been placed in service by August 3rd was less than $176 million. I'm not exactly sure how much less.

COMMISSIONER KONDO: When you're using the term "placed in service," is that different from the way that Ms. Sekimura is using the term?

MR. ISLER: No. What I mean by "placed in service," is plant and service and AFDUC is suspended or stopped.

COMMISSIONER KONDO: Why are you testifying that it's less than 176 when Ms. Sekimura testified it is 176?

I don't understand that difference.

Could you explain that, or Ms. Sekimura, or somebody explain that?

Because I'm getting two different understandings of what was booked to plant and service as of August 3rd; or, maybe I'm misunderstanding your response.

MR. HEMPLING: Could you start with the definition of "plant and service," because the confusion I'm hearing is the difference between the fellow who's managing the project and the person who's managing the books; and, I think the confusion arose because the same three words might have been used in two different ways.

MR. ISLER: Well, let me try first to see if I can clarify this.

All right. I believe that the $176 million was a figure that was taken from my cost report which had explained how much had been expended to date for all project components as of September 28th.

COMMISSIONER KONDO: September 28th or July 28th?

MR. ISLER: The cost report has September 28th.

COMMISSIONER KONDO: Okay.

MR. ISLER: I don't know that anybody in this room right now has the information in front of them what the total expenditures were for all projects on August 3rd.

COMMISSIONER KONDO: No, the reason why I ask the question about the date is because Ms. Sekimura's testimony then it would book to plant and service as of August 3rd, you're talking about the cost report of September of 28th, which is after August 3rd.

MR. ISLER: I believe that there was some confusion when the number was given to Ms. Sekimura on the 176 million.

COMMISSIONER KONDO: Confusion for purposes of what was booked to plant and service or confusion as to what was the response to my question?

MR. ISLER: Confusion as to what was actually booked to plant and service at the time.

COMMISSIONER KONDO: Okay. I'm sorry, I interrupted you.

Go ahead.

MR. ISLER: So, as of September 28th, approximately $176 million had been expended on all components. Any dollars that were attributable to the black start generators or the water treatment system at that time were not booked to service and AFDUC continued on those portions.

MR. HEMPLING: And those costs that you just referred to with respect to black start and water treatment are part of the 176?

MR. ISLER: Any costs that have been incurred for those components at that time were part of that 176, yes.

MR. HEMPLING: That's part of where the confusion is.

So the 176 is total expenditures, some of which, most of which, has been booked to plant and service, some small portion of which has not yet been booked to plant and service as of September 28th; is that correct?

MR. ISLER: That is correct, yes.

COMMISSIONER KONDO: Thank you.

MR. ISLER: Sorry for the confusion.

COMMISSIONER KONDO: Okay. Actually, I didn't intend to spend so much time on the booked to plant and service but thank you for clarifying it.

These are the questions I really wanted to ask, and they really are for Ms. Sekimura, I think.

I wanted to understand what the impact to revenues would be if CT-1 was disallowed?

MS. SEKIMURA: The impact to revenue is based on the 163 million. The average cost is $12 million on an annual basis.

COMMISSIONER KONDO: Do you have a number as to what the impact on revenues would be if the Commission were to use the 193,100,000 figure rather than the 162-million-dollar figure?

MR. WILLIAMS: And to clarify it, if we use an average rate base?

COMMISSIONER KONDO: Correct, using the average rate base.

MS. SEKIMURA: I think an average rate base, that would add approximately $4.

COMMISSIONER KONDO: So about $16 million annually?

MS. SEKIMURA: Approximately.

COMMISSIONER KONDO: Do you know what the ratepayer impact for both of those items?

If CT-1 is disallowed and are using the 162-million-dollar figure which was -- strike that.

If we allow CT-1 to be included in the rates using the average test year concept and 162-million-dollar figure, do you know the impact to residential rates?

MS. SEKIMURA: I don't have that number right now.

COMMISSIONER KONDO: Are you the person that would know that or is that Mr. Young?

MS. SEKIMURA: I believe that's Mr. Young.

MR. HEMPLING: Well, excuse me. But, very roughly speaking, if you're talking about what's the total revenues and the revenue requirement roughly. About a billion?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Okay. So 16 million divided by a billion, you're just looking for rough numbers. Correct?

COMMISSIONER KONDO: Actually, isn't the answer, and maybe I should have known this, isn't the answer looking at the Settlement number and then looking at the interim number and that would be the difference or the impact to a residential ratepayer, because the settlement number included CT-1 at the 162-million-dollar number on an average rate base; is that correct?

MS. SEKIMURA: Could you repeat that, please?

COMMISSIONER KONDO: Sure. I thought, perhaps, that my way was simply Mr. Hempling's way but maybe it's not, because the Settlement was based -- I'm sorry, the Settlement included CT-1, and it was based upon the average test year concept and the number that was used 163 or $162 million, that the interim took out CT-1; so, the difference between the interim and the Settlement number would be the impact on the ratepayers?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: Roughly speaking, because I know that there's other things that were taken out in the interim?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: I don't remember what we called Option 2 when we were talking with Mr. Brosch yesterday about the different alternatives. It was the option where you include the entire amount of the plant and rate base, immediately rather than via the average test year concept.

Do you remember that discussion we had with Mr. Brosch?

MS. SEKIMURA: Yes.

COMMISSIONER KONDO: What's the impact on rates if we include or impact on revenues if we include the entire $162 million, or whatever the number was, that was settled in rates immediately a hundred percent rather than the 50 percent from the average test year concept?

MS. SEKIMURA: You're asking for an impact on rates?

COMMISSIONER KONDO: Sorry, revenues. And, I guess, we called it yesterday the "annualized full recovery."

Is it double?

MS. SEKIMURA: It would be double, so 24 million in revenues.

COMMISSIONER KONDO: Okay. And the answer would be the same with respect to the 193 million if we included in all the rates immediately, double the answer you had given me before, double the 16 million?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: And if I wanted to understand the ratepayer impact of the residential rate period impact of allowing the entire amount into rates would it be roughly equivalent to doubling -- no, I guess it wouldn't.

MS. SEKIMURA: I don't believe it would be a doubling impact.

COMMISSIONER KONDO: Do you know what the impact on the residential ratepayer would be if we allowed the entire amount of CT-1 in rates, whether it's at the 162- or the 193-million-dollar amount; roughly, even a percentage?

And if you're not the right person to answer that question, you can pass. I'm okay with that.

MS. SEKIMURA: I would like -- I don't know the number at the moment.

COMMISSIONER KONDO: Okay. I know in the interim we disallowed CT-1. Correct?

MS. SEKIMURA: That's correct.

COMMISSIONER KONDO: I want to get an understanding of what impact that had on the company vis-a-vis the rating agencies.

Can you talk to me about that?

MS. SEKIMURA: Sure. Basically, a couple of key points from the rating agency standpoint in terms of how they view this, number one, is they take a look at the timeliness of a cost recovery for a large capital investment; and, they also take a look at the regulatory actions that come out in a rate case.

And so some of the feedback that we got from our rating agencies included some concern over the uncertainty as to the timing of the recovery of CT-1 costs. It was particularly concerning to them. As they characterized the CT-1 as a fundamental utility investment, this application was previously approved by the Commission.

They also noted that our credit metric currently are weak to support our current rating of a triple B. And they were concerned that any delay of recovery would further weaken our credit metrics.

We also had conversations. That's conversations we had with S&P and they followed up with publications which they articulated the same message. We also had conversations with the Moody Investor Services, and they were also concerned about the uncertainty as to the timing of the recovery of the costs for CT-1; and, they also asked, specifically, whether the Commission would wait until final decision in order were issued until cost recovery could occur; and, with the uncertainty of that final decision, expressed a lot of concern about that large capital investment that was being made by the company for which no return would be made.

COMMISSIONER KONDO: Do you have discussions, do you, yourself, have discussions with the people with S&P as Standard & Poor's.

MS. SEKIMURA: Yes.

COMMISSIONER KONDO: Was there any representation made as to the expectation of the Commission to include CT-1?

MS. SEKIMURA: Expectation in terms of they're waiting for a --

COMMISSIONER KONDO: Did you provide any information to the Company about -- I'm sorry, to the raters about the Company's expectation as to whether or not CT-1 would be included; and, if so, when it would be included?

MR. HERZ: We provided no expectation, but we talked about the process that we're going through, including the hearings that are being undertaken right now, and we did tell the rating agencies that the decision in terms of cost recovery is left in the Commission's hands; so, they are carefully watching what comes out of the case.

COMMISSIONER KONDO: Anything else relating to the ratings agencies, the impact of the interim decision disallows CT-1?

MS. SEKIMURA: I don't have any further comments.

COMMISSIONER KONDO: What about the impact of the interim decision with respect to the Company's ability to borrow money?

Has this been any impact?

MS. SEKIMURA: Well, I can speak to our recent bond issuance. In July of this year, we went to the market and there was a bit of concern over the negative outlooks that were placed on us by both of our rating agencies. We did secure an interest rate at 6.5 percent for those bonds. And, obviously, if you're a higher rated company the interest rate would have been much lower, but we were able to access the capital market at our current rating.

COMMISSIONER KONDO: If CT-1 had been allowed an interim would you have expected the interest rates to be different?

MS. SEKIMURA: I would not have expected the interest rates to be different because of our current credit rating was maintained; but, I would add that investors do take a look at what's happening on the regulatory space as, sort of, an indication in terms of regulatory support going forward.

COMMISSIONER KONDO: The bonds that you talked about, they were issues by HECO or AGI?

MS. SEKIMURA: The utility.

COMMISSIONER KONDO: I guess I was a little curious as to some of the comments you made about the rate -- your discussions with the rating agencies because, you know, if I look at the interim decision, it talks about what the Company is probably entitled to; and, I think, that was our standard in issuing -- the standard for issuing the interim decisions.

So given that standard, the conclusion, if I was somebody from the outside, would be probably not entitled to recover CT-1 in final rates. You talked to the raters about that or did the raters talk to you about that, the likelihood of recovery?

MS. SEKIMURA: They do talk about that and we talk about the process that we are going through to talk about CT-1 in the hearing.

COMMISSIONER KONDO: Do they have comments about what your process is about what you're -- the way that you're approaching it?

MS. SEKIMURA: Not specifically.

COMMISSIONER KONDO: How frequently do you talk to the rating agencies?

MS. SEKIMURA: The rating agencies, we meet with them on an annual basis where the management team goes up and we talk about our company and the recent events. We also speak with them on the phone periodically; particularly, when there are rating actions that come out that shows an interim decision or an important milestone in the Company; and, so we do keep in contact with them on a regular basis.

COMMISSIONER KONDO: And the discussions that you were describing that you had with the rating agencies after the interim was that by phone or was that during the annual meeting that you had with them?

MS. SEKIMURA: That was by a phone. We actually met with, in person, S&P right after -- right in the midst of the Settlement. And, at that point, we talked about what was happening with our HECO 2009 rate case. And following that discussion and taking a look at our credit metrics and the timing of a possible decision in the case, they put us on negative outlook.

When the interim decision and order came out, we had another conversation with them over the phone, and we talked about what was included in the interim decision and what was not included, and, they did not take any further action. What they did note was the actions that they took previously with the negative outlook had incorporated or anticipated uncertainly on the decision and what was going to be in there.

MR. ALM: Commissioner Kondo, I was also on both of those phone calls and, you know, I would like to respond to one part of what you asked.

They did not read it that we would not get a recovery for CT-1. What they read was that you had questions that we needed to answer in the subsequent hearing that you specifically asked us to provide further information and that there would be a hearing on this issue.

I think if they actually felt that a 160- or a

190 million-dollar unit would sit on our books unrecovered for either period, or for a significant period of time, the reaction, I think, would have been devastating to our rating, I think.

I mean, I don't know where they'd go; but, you know, they're assuming that we will be able to demonstrate to the Commission that it is used and useful and that we have met the concerns the Commission raised in that interim order. I think they honestly felt that you were saying there was no likelihood of recovering on a 200-million-dollar investment, you know, the street's reaction would be -- I think would be horrendous.

COMMISSIONER KONDO: Did you ask them about what the reaction would be if it wasn't (inaudible)?

MR. ALM: I think the way it actually came up is, you know, more a statement by them, Does this mean the Commission has said no, period, and we don't reach a decision that way.

COMMISSIONER KONDO: I guess I'm just trying to get some context upon your statement that it would be devastating.

Is that a statement that they made in response to your question; or, is that just your impression of what was represented?

MR. ALM: I don't know that they used that terminology, but they said something to the effect we can't imagine you're not ultimately getting a recovery for it since you've built it pursuant to a Commission decision in order and it is in service.

You know, we talked about the issues that you raised. One is as of the date of the decision it actually wasn't yet in operation. So your issuant decision at the beginning of July meant the unit actually was not in service.

And, secondly, you raised issues about the biofuel. You know, and what we said was, one, it is in -- it will be in service by the time that we get before the Commission, and, two, we're going to move aggressively to deal with the biofuels concern, and we believe we can also satisfy that by the time we get to the hearing and be able to show the Commission that we're back on track.

COMMISSIONER KONDO: When was the discussion that you had with the rating agencies?

Do you recall, roughly? A month?

MR. ALM: July.

COMMISSIONER KONDO: I just want to say that, you know, I understand and appreciate the financial impact of the CT-1 to the Company. I do. And I do appreciate the discussion that we had yesterday with Mr. Williams and the Company folks and the CA folks on the used and useful issue.

Now it was a very enlightening discussion; but, I got to say that the Company has put us in a very challenging position to find that it's used and useful. I understand the financial impact, but I just wanted the Company to understand that it seems, to me, you're putting us in a very challenging position. The stipulation is not crystal clear as to whether not there was a contemplation to use petroleum diesel before the air permit was modified or before bio-diesel was available. We had the discussion yesterday.

I think that from the Imperium order I think that -- I hope the Company understands that the Commission didn't think that was a good contract; and, from my perspective, I think there's some inconsistencies as to the Company's statements and the Company's actions, you know, regarding what was contemplated in the stipulation regarding whether or not the plant would be able to run on petroleum diesel.

Because of all that, I think you guys have put us in a very challenging spot, but I do understand the impact and I appreciate the information from you Mr. Alm and Ms. Sekimura about the financial impact.

Thank you.

CHAIRMAN CALIBOSO: Mr. Hempling.

MR. HEMPLING: Yes, we're going to turn to some questions on the pipeline.

So we're off CT-1 and on to the KBTH pipeline.

Good morning, Mr. Morikami.

MR. MORIKAMI: Good morning.

MR. HEMPLING: And, I sorry, I can't see your name card.

Ms. Nagata --

MS. NAGATA: Good morning.

MR. HEMPLING: -- what are your individual responsibilities with respect to this KBPH pipeline?

MR. MORIKAMI: I was the witness.

MR. HEMPLING: Sir?

MR. MORIKAMI: I'm sorry.

MS. HIGASHI: Please, use the mike.

MR. MORIKAMI: Good morning. Ken Morikami, Manager of the Engineering Department in the energy delivery side of the business.

I was the witness in the 2007 rate case on covering property held for future use.

MR. HEMPLING: And besides being a professional witness, what's your responsibility for the Company?

MR. MORIKAMI: Being a Manager of the energy department -- Engineering Department and Energy Delivery, we handle engineering design and project management of major capital projects?

MR. HEMPLING: And Ms. Nagata?

MS. NAGATA: Good morning. I'm the Treasurer and Manager of Treasury and Financial Services for Hawaiian

Electric Company; and, I sponsored testimony T-17 in this current case.

MR. HEMPLING: Okay. So, Ms. Nagata, how long has this pipeline been in rate base?

MS. NAGATA: This pipeline has been in rate base since it was installed in 1991.

MR. HEMPLING: Mr. Brosch, are you familiar with this issue?

Mr. Carver, are you familiar with this issue?

MR. CARVER: Yes, I am.

MR. HEMPLING: Have you ever heard of a piece of property being in rate base for 17 years on the basis of property held for future use of 17 years?

MR. CARVER: I have to say that this one is unusual in that respect.

MR. HEMPLING: My question is, Have you ever heard of one?

MR. CARVER: Not other than this particular piece of property.

MR. HEMPLING: Can you imagine the rationale for having a piece of property in rate base for 17 years a plausible rationale that's consistent with any regulatory principle?

MR. CARVER: In the Company's 2004 rate case, I actually did some discovery on this subject; and, the Company provided a copy of a feasibility study that they prepared at the time they decided to spend the money for this project, and the rationale was to provide the Company alternatives for future use of that pipeline for petroleum --

MR. HEMPLING: Excuse me. If you could listen to my question carefully.

Their rationale is in their testimony.

MR. CARVER: Yes.

MR. HEMPLING: I'm asking whether you understand there to be rationales in general for a piece of property staying in rate base for this amount of time under the principle of property held for future use.

MR. CARVER: Only to the extent that it's continuing to convey a current economic benefit to the Company. In this case, the Company contends that its value is through continued negotiation with petroleum --

MR. HEMPLING: Right.

MR. CARVER: -- suppliers.

MR. HEMPLING: I'll come to that. I'm trying to get the regulatory principles in place so the Commissioners can understand how to apply them and what to apply as they make a decision on this.

Let me turn to a finance issue with you, Mr. Carver. It being a rate base, meaning it's been earning a return, but it's not been depreciated; so, the return is being earned but no recovery is occurring; is that correct?

MR. CARVER: That's correct.

MR. HEMPLING: Do you have any opinion as to -- well, if I were to ask you whether after 17 years with whatever rate of return the Company has been earning over this period of time, do you have some opinion as to whether the financial effect for Company is above, below, or equivalent to what would have happened if the whole thing had been rate based and depreciated and had been made whole for it?

Any feel for that?

MR. CARVER: Generally, assuming, a 10 percent pretax return, which, I think, is conservative over 17 years, this particular project has an investment of about a half-a-million dollars. That would translate into about $50,000 per year in revenue requirement; so, over a 10-year period, that would translate into a half-a-million dollars worth of recoveries from ratepayers so --

MR. HEMPLING: And over a 17-year period --

MR. CARVER: Well --

MR. HEMPLING: -- you'd get another.

MR. CARVER: -- 350,000 over the following seven years.

MR. HEMPLING: Okay. So you figure, at this point, the Company has picked up about $850,000 based on this item?

MR. CARVER: Yes, in terms of return recovery.

MR. HEMPLING: So how does that compare with making the Company whole with respect to a typical depreciation rate and full recovery of the cost and recovery on the unamortized portion over the period of time?

I mean, if the Commission were to say it's coming out now and it's never coming back in again, would that be a bad hair day for the Company or would be they be able to say, Well, we pretty much earned what we expect for this investment?

MR. CARVER: I don't think the amount is material enough for it to be necessarily be a bad hair day for the Company. An asset of this type probably would have a 25- or 30-year life that would translate into maybe a 3-percent book depreciation rate; so, we would be about halfway roughly through the assets used for (inaudible); so, we would have a declining net plant balance had it been rate based as a plant and service item.

MR. HEMPLING: I guess maybe the only way to ask you the question is to have you compare it to net present values, the net present value of the returns that they've received over time under the current treatment as compared to the net present value of the dollars that they would have derived if we had gone through this in a normal approach.

I mean, can you advise the Commission at all as to whether putting aside magnitude whether this would be a poor decision by the Commission to take it out, just on financial grounds before we get to the rationales for its inclusion?

MR. CARVER: My personal opinion is that there has been adequate compensation over the years. I'm not aware that there's an immediate plan for outlook to use that pipeline to place it in service.

MR. HEMPLING: I'm coming to the purposes in a moment. I'm just asking a financial question. I think I understand your answer.

MR. CARVER: Okay.

MR. HEMPLING: All right. Now are you familiar with the Company's rationale?

And I'll come to you, ladies and gentlemen, in a moment.

But are you familiar with the Company's rationale for why it should remain in rate base at this time?

MR. CARVER: Generally, yes.

MR. HEMPLING: Well, how about specifically?

Are you familiar with this argument that there's an actual -- are you familiar with the fact that they have made a confidential calculation with respect to its value and bargaining?

Are you familiar with that confidential calculation?

MR. CARVER: I have not seen that confidential calculation.

Do you have an RFI response?

MR. HEMPLING: I'm not sure I want to take up hearing time on it at the moment, but I may decide to in a the second. Also, I don't want to put you on the spot if you haven't studied it because it's got about six layers to the calculation here.

MR. WILLIAMS: And I think this was the same analysis filed in the 2007 rate case and Mr. Carver looked at that.

MR. HEMPLING: Okay. In fact, if that is correct -- well, do you remember the analysis that was used in 2007, let's say, it's a matter of taking a rate of return, applying it to the investment and then using a -- what they call a "discretionary element adder" to describe what the effect on fuel costs to describe the contribution to saving and fuel costs.

Do you recall that at all?

MR. CARVER: I have a general recollection of it, but I don't recall the specific details of that calculation.

MR. HEMPLING: But you testified against it in 2007 you said?

You found it to be -- I'm sorry, you testified against it?

MR. CARVER: No, I don't believe I filed testimony opposing its rate base inclusion.

MR. HEMPLING: Okay. Ms. Nagata, are you familiar with the confidential calculation to support the Company's argument for the continued inclusion of this investment rate base?

MS. NAGATA: I'd like to pass to Mr. Murakami.

MR. HEMPLING: Okay. Mr. Murakami, are you familiar with the calculation?

MR. MORIKAMI: Yes, I am.

MR. HEMPLING: Okay. I think I have a pretty, simple question and I don't mean it to be argumentative. I just want to try to do this without having to shut the doors and turn the lights off.

Is your calculation assuming that the entire savings in terms of purchase of low sulfur fuel is attributable to the existence of this pipeline?

MR. MORIKAMI: No.

MR. HEMPLING: Sir?

MR. MORIKAMI: No.

MR. HEMPLING: Okay. Go ahead.

MR. MORIKAMI: If I could explain.

MR. HEMPLING: Please.

MR. MORIKAMI: Generally, what we try to do is to come up with an analysis to show that it is beneficial. It was a prudent investment and a benefit to keeping this in property of future use. It's -- it was hard to quantify. In my testimony, it was -- it was hard to quantify it, but what we tried to do here was based on the revenue requirements for that half-a-million-dollar investment, and due to some good negotiations with the suppliers, we looked at the estimated savings, total savings, over the past, I believe, few years; and if we just -- 10 percent of those savings, it equates to more than the revenue requirements; so, that's what happened in that analysis pretty much.

MR. HEMPLING: So would it be a misunderstanding in your analysis to say that you assumed that the entire difference between the 1998 and 2007 discretionary element entered prices could be attributed to the existence of the pipeline?

That would be a misunderstanding of your calculation?

MR. MORIKAMI: Yes, that would be a misunderstanding.

MR. HEMPLING: Well, how would you correct it?

MR. MORIKAMI: It would be a representation that about 10 percent would be of the total estimated savings of the -- it would be 172,000. It would be more than -- it would be more than the revenue requirements.

MR. HEMPLING: Ms. Nagata, did you hear Mr. Carver's discussion with me about the adequacy of compensation?

MS. NAGATA: Yes.

MR. HEMPLING: Do you have any disagreement with his statements about the adequacy of compensation?

MS. NAGATA: I agreed that the calculation that he made represents the revenue requirements or the revenues that we have collected over that period of time.

MR. HEMPLING: Right. I'm asking you do you agree with him that you've been compensated adequately for this investment?

MS. NAGATA: Yes.

CHAIRMAN CALIBOSO: All right. This completes Panel 5. And, again, at the end of each panel, we give the parties an opportunity to question each other or cross-examine each other; so, I would like to do that right now.

Mr. Williams?

MR. WILLIAMS: It was just a simple clarification question.

When we look at trying to compare a situation property held for future use is not depreciated versus property that's in plant and service and is depreciated, the depreciation element is returned to shareholders and they have that opportunity to reinvest that element; is that correct?

MR. CARVER: Yes, that's a fair statement.

MR. WILLIAMS: But if we were going to do a net present value comparison of the two scenarios, you would have to take into account the opportunity to reinvest the return of the investment; isn't that correct?

MR. CARVER: I would not perform that net present value calculation in that manner.

MR. WILLIAMS: But if you're going to compare the opportunity to earn on an investment between two different scenarios, you got to take into account the total picture, don't you?

MR. CARVER: Certainly. Under one scenario, you would look at the amount included in rate base is plant held for future use over a specified term and determine the net present value of that revenue -- annual revenue requirement of fact.

The other scenario you would be looking at a declining depreciated investment in rate base plus the recovery through depreciation also then on a net present value basis to evaluate the net delta between the two scenarios.

MR. WILLIAMS: And investment return through depreciation is typically reinvested by shareholders and other assets in the rate base?

MR. CARVER: It could be. It may not be.

MR. WILLIAMS: Or they invested in their own investment?

MR. CARVER: It certainly could. It could be paid out in the form dividends.

MR. WILLIAMS: Thank you. That's all the questions that I have.

CHAIRMAN CALIBOSO: Mr. Itomura, any questions?

MR. ITOMURA: The Consumer Advocate has no questions.

CHAIRMAN CALIBOSO: Mr. McCormick?

MR. MCCORMICK: The Department of Defense has no questions.

CHAIRMAN CALIBOSO: Thank you.

Mr. Williams, are you folks ready for the next panel, or we can take our morning break earlier?

MR. WILLIAMS: I would suggest we take a break and find out whether they're in the hallway, because there was no place in here for them.

CHAIRMAN CALIBOSO: All right.

Let's reconvene at 10:20.

We are in recess.

(Whereupon, at 10:03 a.m., a recess was taken, and the proceedings resumed at 10:20 a.m., this same day.)

CHAIRMAN CALIBOSO: Good morning, again.

I'd like call this proceeding back to order.

We are starting another panel, Panel 6, the Sales Decoupling and ECAC.

Mr. Hempling -- oh, Mr. Williams, I guess you can start by noting your witnesses appearances, please.

MR. WILLIAMS: Yes, mr. Chairman. We have five witnesses for this panel. Mr. Hee, who has previously been sworn in. Kathy Hazama, who will be -- who has taken the place of George Willoughby in this docket on sales. She has not been sworn in yet. Jeff Makholm, from National Economic Research Associates, has not been sworn in yet. Ross Sakuda is here in the event that there's a heat rate question; and, Tayne Sekimura. So we have two new witnesses to be sworn in.

CHAIRMAN CALIBOSO: Thank you.

Stand please. Do you solemnly swear or affirm that the testimony you're about to give will be the truth, the whole truth, and nothing but the truth?

ALL WITNESSES: Yes.

CHAIRMAN CALIBOSO: Thank you. You may be seated.

And all the other witness have been sworn in. Correct?

MR. BROSCH: Correct.

MR. WILLIAMS: Mr. Chairman, we do have those sales exhibits that Mr. Matsuura can pass out. These were previously provided to the parties. I actually talked to Mr. Hempling before, whether it would be helpful because it shows whether the forecast had have been high or low on a consistent basis.

CHAIRMAN CALIBOSO: Okay. Have the other parties seen them?

MR. CARVER: Yes.

CHAIRMAN CALIBOSO: And are there any objections?

MR. ITOMURA: The Consumer Advocate has no objections.

CHAIRMAN CALIBOSO: Mr. McCormick?

MR. MCCORMICK: The DOD has no objection.

(HECO Hearing Exhibit Nos. 1 through 3 were marked for Identification.)

CHAIRMAN CALIBOSO: I'd like for you to describe them.

MR. WILLIAMS: This Hearing Exhibit 1 is a Year-Ahead Sales Forecast Accuracy. It's a chart that shows the actual versus the deviation of the actual versus the forecast on a the Year-Ahead basis, and the numbers that go into that are shown on page 2 of that exhibit.

The second exhibit which looks like a modern arts drawing. It just shows the whole -- the various sales forecasts versus where the actuals have gone and it also shows the trends.

The third one shows the forecast that's been used in the test year versus the actual results for each month. The results for the first six months is public information now since we filed in the 10-Q for two quarters. The information that's blacked out is the actual results for July, August, and

September. We can speak to that without going in camera if we speak in generalities; but, as of Monday, that will no longer be confidential information because we will be filing the third quarter 10-Q on that date.

CHAIRMAN CALIBOSO: Thank you, Mr. Williams.

So this is under HECO's cover letter dated October 20, 2009, and attaches prehearing exhibits, Hearing Exhibit 1, Year-Ahead Sales Forecast Accuracy. And Exhibit 2, Sales Forecast; and, Hearing Exhibit 3 Actual Sales Versus September 2008 Update. Correct?

MR. WILLIAMS: That is correct, Mr. Chairman.

And we have one errata in Jeff Malcolm's testimony that he pointed out to me just now. This is ST-10B. This is page 29.

I'll read it into the record, but if anyone has a question, you can ask Jeff.

This is on line 1, The 64 percent should be 66 percent, and, it then says up from 37 percent, it should be up from 52 percent.

CHAIRMAN CALIBOSO: Any questions?

Any other questions, Mr. Williams?

MR. WILLIAMS: I hope that's it, Mr. Chairman.

CHAIRMAN CALIBOSO: All right.

Mr. Hempling?

MR. HEMPLING: Thank you, Mr. Chairman.

This Panel 6 focuses on decoupling; and, then the ECAC. So let's start with an understanding of the decoupling issues.

What I'd like to do in this decoupling discussion is explore for the Commission the range of interactions between the Commission's range of possible decoupling decisions in this rate case. Procedurally, as everybody knows, both cases are pending, which means that the rate case could be decided before the decoupling case, the decoupling case could be decided before the rate case; or, the two cases could be decided simultaneously.

And the purposes of this set of questions, I think, is not non-argumentative, it's to make sure the Commission understands fully all of the possible interactions so that it doesn't have to repeat decision-making in either of those two dockets unnecessarily.

Mr. Brosch, were you involved in the decoupling case?

MR. BROSCH: Yes, sir.

MR. HEMPLING: What role did you play there?

MR. BROSCH: I was representing the Consumer Advocate in the development of preliminary and final statements of position and in the negotiation of what ultimately became a joint statement of position with the HECO Companies and assisted the Consumer Advocate in answering information requests and appearing here before you.

MR. HEMPLING: Okay. We're going to use you as the horse to ride here, if you don't mind.

And this is not a time where I want to be leading you. I'd rather it be the other way around. Let's identify all the ways -- let's, first, start on the revenue side and then go to the costs side and identify the ways in which adoption of decoupling by the Commission could affect the revenue expectations that are part of the rate case.

Are you following my question?

MR. BROSCH: I think so. Let me start talking and you can tell me where else you'd like to go.

MR. HEMPLING: All right.

MR. BROSCH: First --

MR. HEMPLING: Excuse me. What we're going to try to do, sir, is make a list of the issue areas and then we're going to delve into each one. I want to get a sense of the full context first; is that okay?

MR. BROSCH: All right. Let me try it this way.

A result of the rate case will be an authorized base revenue level which will be a target revenue level for purposes of the Revenue Balancing Adjustment, the RBA tariff, if it were approved; and, all of this I'm going to say with the caveat, "if it's approved."

Then with respect to the balance of the income statement, the Commission's order here will contain findings with respect to O&M expenses that will serve as the starting point for application of labor and nonlabor escalation rates if a RAM tariff is approved that uses that starting point.

With respect to rate base, the rate adjustment mechanism builds rate base primarily from recorded information at the end of the prior calendar year plus prescribed calculations for major projects and general plant additions to estimate four elements of rate base at the end of that year.

Then a differencing occurs comparing that calculated RAM year rate base to the awarded rate base for purposes of determining the incremental return requirement from RAM rate base relative to what was last authorized for in the first filing in the '09 test year.

There would also be a calculation of depreciation expense using the end of the prior year's recorded plant and service balances and applying Commission-approved depreciation accrual rates to get that depreciation expense element for the RAM year that would compare to the depreciation expense embedded in the rate order to get that delta for revenue requirement purposes.

Now those are -- let me turn then to Mr. Carver, but those are the significant components of that proposed mechanism and how it interacts with the rate order.

MR. HEMPLING: Anything to add, Mr. Carver?

MR. CARVER: Yes. I would just comment that with respect to the RAM rate base element Mr. Brosch made reference to some actual investment levels that was accurate, but for limitations on the major projects that have been approved by the Commission, they would be limited to the Commission-approved values for that component calculation.

MR. HEMPLING: Okay. I think, gentlemen, everybody understands then how decisions in the rate case get plugged into the decoupling process.

What I want to explore now is to what extent could decisions in the decoupling case effect the appropriateness of numbers the Commission determines in the rate case.

Just starting with the revenue level, Mr. Brosch, is there anything that the Commission could decide in a decoupling case that would render their revenue levels assumed for purposes of the rate case to be inappropriate?

MR. BROSCH: I believe that your panel on rate of return will touch heavily on the issues of operational risk effects associated with the approval or disapproval of decoupling. That's one obvious place where there will be interaction.

MR. HEMPLING: Right. Excuse me. I'm going to set aside that ROE issue for -- well, maybe a half-hour from now, but I got that one.

MR. BROSCH: Okay. Beyond that, I would observe that in our settlement in the rate case we have adopted and reflected the lower sales forecast that was included in the company's December update filings; and, by doing so, we have captured much of the recent decline in sales volumes in calculating the revenue requirements; so, as indicated in the supplemental testimony, there's really no further adjustment required to sales volumes or revenues at present rates, because the settlement has already captured that decline.

MR. HEMPLING: Well, was there anything about the decoupling situation that would -- is there anything about a decoupling decision that would affect the amount of kWhs that customers purchase?

MR. BROSCH: The decision would likely not in any way directly affect sales volumes, you know, barring some distant relationship between prices and price elasticity, I wouldn't expect there would be an effect.

MR. HEMPLING: Well, the customers see the same rates under decoupling. It's just they have to pay a true-up at some point after the month of their consumption. Correct?

MR. BROSCH: There would be the effect of the true-up through the RBA that you spoke of; and, that's really what I had in mind when I said there may distant price changes and price reactions by customers; but, for that, I don't see any linkage to sales volume.

COMMISSIONER KONDO: Can I follow up on that?

MR. HEMPLING: Go ahead sir.

COMMISSIONER KONDO: Looking at the information that the Company provided us just now as to the actual declining sales, which would result, as I understand it, the decoupling increase in the customer bill; and, I know that for the decoupling docket we separated residential and commercial but I'm just talking in general.

Is that correct, declining sales would likely result or will result in an increase in customer bills?

MR. BROSCH: Yes, the tracking is done in revenue dollar terms but what you said is correct. If there were persistent declines in sales and revenues relevant to target revenue levels, that would build a cumulative RBA balance that would then come back as a required surcharge to customers when you next reviewed that mechanism and approved those rate changes.

COMMISSIONER KONDO: So that means if I use the same amount of kWh my bill is higher than it is today, field price aside.

MR. BROSCH: If you and all your neighbors do that, yes, that's the effect. The revenues are pooled for the entire revenue requirement to calculate.

COMMISSIONER KONDO: And that's a good point, because there's some people that might take other type of energy efficiency measures or conservation which would cause those people who don't do that their bills to, perhaps, increase even more. Correct?

MR. BROSCH: That's correct. There's still an award for conservation to you as an individual customer.

COMMISSIONER KONDO: Because of that scenario where bills will go up, now whether or not you are doing conservation, energy efficiency, assuming the same usage, given the declining sales, assuming declining sales continuing, don't you expect there to be less sales if we have a decoupling mechanism in place because of the price, because of the cost impact to the residential user, don't you expect sales to decline?

MR. BROSCH: If your question goes to that price elasticity notion that I spoke of earlier, yes, I would expect there to be some effect like that, that customers would react to prices that would be higher with RBA and RAM than without and might have a stronger incentive to find opportunities to conserve.

COMMISSIONER KONDO: And I apologize and maybe I either jumped the gun or didn't understand your response to Mr. Hempling, but I thought you had said that the settlement captured a lower sales forecast; and, because of that, you didn't expect there to be any difference if the decoupling mechanism was implemented by the Commission.

MR. BROSCH: Let me clarify.

COMMISSIONER KONDO: Please.

MR. HERZ: The Company filed initially with a sales forecast for the test year that, as events unfolded, it became obvious that the sales forecast was not going to be achievable in 2009; so, in its December update filings back in December of '08, a proposed modification to that prefile position was submitted by the Company that reflected significantly lower assumed sales for the test year; and, the Consumer Advocate, in its prefile evidence, and then in the Settlement Agreement, agreed to use that lower forecast; but, it's still a fixed or set amount of kilowatt hours and revenues at present rates that gets baked into the revenue requirement, and assuming you approve it, and then becomes the target revenues subject to any RAM or other adjustment for purposes of RBA tracking in future periods.

COMMISSIONER KONDO: What were the assumptions that you had at the time that you accepted the lower sales forecast?

And what I mean by that, were you accounting for any specific decline because of decoupling or was it just the expected sales given the current system that the current regulation that we have in place?

MR. BROSCH: There was considerable information submitted by the Company with that revised sales forecast that we looked at. That consideration was not really driven by decoupling at all. It was driven by current knowledge of economic conditions. It was driven by observable trends and actual monthly kilowatt hour sales that made a compelling case that the original forecast was not very useful or likely to be indicative of actual sales in the test year.

COMMISSIONER KONDO: Okay. I'm sorry, because I'm fumbling with these questions because that was actually what I thought the lower forecast had it been. It had been reduced because of the economic times that had changed since the initial forecast was made.

MR. BROSCH: Yes.

COMMISSIONER KONDO: Correct. Right?

MR. BROSCH: Yes.

COMMISSIONER KONDO: So it had nothing -- it did not take into account the decoupling per se. Correct?

MR. BROSCH: It did not account for decoupling in any way, that's correct.

COMMISSIONER KONDO: So, I guess, my question is you expect decoupling to further reduce the volume of sales?

And, I'm sorry, because that was my initial question.

MR. BROSCH: Well, let me respond more completely. Maybe I shorthanded that too much. I jumped to something I said earlier about a potential effect from decoupling being higher prices in the future than would otherwise occur without decoupling and the potential for there to be some price elasticity response by consumers to that effect. I don't think that's as an important a driver as other things that affect the company's future sales like economic conditions in general.

COMMISSIONER KONDO: Does that mean that you don't think that it's an important enough factor for it to require an adjustment to the sales, through the forecasted sales, is that what you're saying?

MR. BROSCH: That's what I'm saying that there's no justification for anticipating and making incremental adjustment to the test year sales for decoupling.

COMMISSIONER KONDO: And what's the basis for that conclusion?

Do you have other research that you've done in other decoupling jurisdictions or is it just your gut feeling?

MR. BROSCH: It's based on my experience and knowledge that, you know, if you look at historical trends and usage per customer and reasonable expectations of future usage per customer, given the conservation effects that we observed and the historical data, and you combine that with expectations regarding numbers of customers, remember kilowatt hour sales, they're a product of how many customers you're serving and how much of those customers are going to use individually and collectively.

It's a much larger dynamic when you look at it in those overall terms than saying in isolation here's a potential price elasticity effect, feedback effect from decoupling, a much more propound effect will be, for instance, future fuel prices and how ECAC will touch customer bills.

COMMISSIONER KONDO: Just talking about -- excluding ECAC and fuel pricing, have you done any type of calculation of modeling when you look at the declining sales forecast that the Company has provided or even using the actuals and determine the increase to customer bills based upon just the declining sales forecast if the Company was implemented, what that dollar impact would be to residential customers and, therefore, using that number to figure out whether or not your conclusion that the change in sales volume or that increase in price because of the change in sales volume will not cause or is insignificant?

MR. BROSCH: The short answer is no. The long answer is there are other much more important variables that would drive expectations of future sales than a feedback effect from decoupling driven price changes.

COMMISSIONER KONDO: Okay. Thank you.

MR. BROSCH: Sure.

MR. HEMPLING: Mr. Brosch, we've been talking about the price effect of decoupling, but I wonder if that's the best term, the price to the customers the same for electricity they consume, it's just that there's a charge that will reflect the true-up periodically. Correct?

MR. BROSCH: I'm not sure if I understand your question. If you mean the Company will collect the same total revenues irrespective of volume, I think I can agree.

MR. HEMPLING: When you use the word "price effect," what are you referring to?

MR. BROSCH: I was referring to an expectation if we think the future holds declining sales, persistent declining sales, that the trend in decoupling adjustments will be positive incremental price changes per kilowatt hour on a customer's bills, then any given customer will look at that; and, if they're sensitive to price, might react with more conservation or measures taking to reduce usage.

MR. HEMPLING: That's a price per kWh because it's a separate decoupling charge that would appear as a per kWh's charge.

MR. BROSCH: That's correct.

MR. HEMPLING: Okay. Because setting aside the decoupling charge, the per kWh price is not recovering charges on change by decoupling. Correct?

MR. BROSCH: That is true but it's changed for ECAC and other things more profoundly; but, yes, that's true.

MR. HEMPLING: Yes, that's why I want to understand.

Let's assume for a moment that there is some type of sales decline as a result of decoupling of the magnitude, the small magnitude that you're anticipating, other than -- now let's look at the effect on the Company's cost, again, to assess whether their cost expectations underlying the rate case could turn out to be inappropriate under a decoupling regime -- other than fuel costs productions associated with generating fewer kWh's, is there likely to be any variability to any other costs as a result of a change in sales of the magnitude that you think might occur or other remaining variable costs effectively non-variable with such a small change in sales?

MR. BROSCH: Well, let me respond this way and see if I'm getting to it.

Beyond fuel and purchase energy costs, which are generally recoverable through the ECAC, the balance of the Company's expenses are largely not variable with kilowatt hour volumes.

MR. HEMPLING: So they'd be uneffected by any sales, so the costs that are assumed for purposes of the rate case, would be unchanged by any decline in sales that arose because of the implementation of decoupling?

MR. BROSCH: That is generally true. There are some instances where portions of production operating expenses are variable with sales, but the dollars are not significant.

There may be feedback effects through uncollectibles, for example, that would vary with sales volumes, customer bills, and uncollectible tendencies, but those are not individually large effects, I'd expect.

MR. HEMPLING: Explain again. I know you just said it wasn't going to be large, but the uncollectibles effect from decoupling is what?

MR. BROSCH: From decoupling specifically, I don't I think you can say there is an effect, but, generally, uncollectibles vary with revenue levels and economic conditions and whatever effects customers' ability or propensity to pay their bills from time to time.

MR. HEMPLING: Well, I guess, the theory would be if sales declined, then there's fewer people, hang fewer dollars, so uncollectibles might decline, is that possible?

MR. BROSCH: It's possible, yes. If we focus on the relationship between uncollectibles and revenue levels and revenues go down, then one might expect uncollectibles to go down. There's more involved than just revenue levels and that, in fact, has been an issue between the HECO companies and the Consumer Advocate in recent cases.

MR. HEMPLING: But in this uncollectibles area, we're going to territory label insignificant in terms of the cost?

MR. BROSCH: Certainly, in the context of what we've been talking about, yes, I would agree.

MR. HEMPLING: What about working capital, is there any potential effect on the Company's work and capital needs associated with the implementation of decoupling?

MR. BROSCH: Probably, not, because the proposed RBA included a 6 percent carrying charge on the balance with the expectation that incremental working capital effects would be accounted for during that carrying charge rate.

MR. HEMPLING: Give me that answer, again, would you?

MR. BROSCH: Yes. The RBA that's proposed as a 6 percent carrying charge rate applied to whatever balance is accumulated, positive or negative, and the effect of that carrying charge rate is to account for the working capital considerations of decoupling so that the regular working cash we consume ourselves within rate cases need not be recalibrated for RBA balances, for example.

MR. HEMPLING: So if the Company's need for working capital is reduced by decoupling, that reduction is going to be reflected in the payments that are not -- it's going be reflected in the bill calculations that flow from decoupling?

MR. BROSCH: Yes, the RBA balance will accumulate nominal dollars and a carrying charge at 6 percent. It would account for the capital costs associated with financing that balance, be it a positive or negative.

MR. HEMPLING: Have you ever thought about the relationship that decoupling might have on the costs the Company incurs for its remaining energy efficiency activities or its DSM activities?

Do you see any possible relationship there?

MR. BROSCH: I haven't thought about it and no relationships occur to me as I start to think about it.

MR. HEMPLING: Well, would an argument be -- and, again, you can tell me if this is in the territory of insignificance, an argument would be that if there were the type of sales reductions that you and Commission Kondo theorized that, as a result of those sales reductions, there would be less need for DSM expenditures or less need for energy efficience expenditures, are we now in the realm of not just the significance but speculation; or, do you have any comment?

MR. BROSCH: I don't have a comment. I'm not particularly close to the analysis that's been done with respect to energy efficiency and DSM program review and approval and would rather not void into that unfamiliar area.

MR. HEMPLING: Other than ROE, can you think of any costs that we haven't discussed that potentially could be effected by a Commission decision on decoupling such as -- so as to require the Commission to revisit the decisions it makes in the rate case?

MR. BROSCH: No, nothing comes to mind.

COMMISSIONER KONDO: What about employee expense for the Company?

Would the Company require additional employees to oversee the RBA and the RAM mechanisms if the Commission approves both, monitor, oversee, whatever?

I thought I had saw -- and, in fact, I thought saw some testimony that there was one position, that was the decoupling position and, maybe, I'm wrong about that.

But from your perspective, is there additional employee costs that the Company would incur?

MR. BROSCH: Perhaps. Although, when we talked about the administrative costs that come from approval of decoupling, the discussion has often turned to the but-for scenario, you know, but-for decoupling would we instead be filing and prosecuting rate cases and doing other things that might be even more costly.

There was care and attention given to the design of a less complex and hopefully more administratively workable decoupling solution; largely, at the urging of the Consumer Advocate, anticipating a number of those filings to review on top of everything else the Consumer Advocate does but, certainly, with sensitivity to burdens that reside here.

COMMISSIONER KONDO: I'm not sure what the answer was.

Is that given the alternative that -- alternative being more readily expensive and more frequently in rate cases, any additional costs associated with employees -- Company employees having to deal with a decoupling RBA and RAM mechanism or a wash or perhaps or to the benefit of the -- it's covered in the rate case; in other words, in the numbers they've already provided?

MR. BROSCH: Yes.

COMMISSIONER KONDO: Did I understand you to say that?

MR. BROSCH: I think that's all true. With regard to the staffing, you know, there clearly are some staffing increases contemplated in the test year that were discussed the other day that involved some of the work required by the Company to process regulatory matters; and, on balance, our view was that the net burden of administering a decoupling should be less than the burden of processing more frequent rate cases, both for the Company and other parties in the Commission.

COMMISSIONER KONDO: Okay, thank you.

MR. HEMPLING: Anything -- anybody in the Company wants to air or do you like where the record stands right now on this topic?

Don't complicate it, Mr. Hee.

(Laughter.)

MR. HEE: There was discussion on what the impact of the RBA might be on the customers' bills in doing a rough calculation, and there were certain assumptions that the sales reduction that we have seen year-to-date in June continues for the rest of the year; and, if the RBA, in fact, has been in place from the beginning of 2009, we believe that the impact on the customer's bill per month for someone who is using 600-kilowatt hours a month, just about 95 cents, unless I believe that number supports the Consumer Advocate, and our contention that the implementation of the decoupling will not have a significant effect on the customers' usage because 95 cents, when compared to a bill, a current bill of the 600-kilowatt-hour resident per month, which is about $147, is not very large in comparison to that total.

MR. HEMPLING: Is that it?

MR. HEE: I did want to --

COMMISSIONER KONDO: Can I ask you a question then, Mr. Hee?

MR. HEE: Yes.

COMMISSIONER KONDO: What's the impact -- I know you guys use the 600 per month -- 600 kWh number always, but I understood yesterday and from the filed testimony, the average user is 654.

MR. HEE: Yes.

COMMISSIONER KONDO: What's the average residential impact?

It might be just pennies more.

But could you tell me that figure, if you have it?

MR. HEE: That would be 50-kilowatt hours more per month.

Thank you.

COMMISSIONER KONDO: Is it basically just one cent more?

MR. HEE: Yes, it's going to be a dollar, three, instead of 95 cents.

COMMISSIONER KONDO: Okay, thank you.

MR. HEMPLING: Is that it?

MR. HEE: That's all.

MR. HEMPLING: Okay. Let's turn to the turn on equity. I know there's an ROE panel next week, but do we have anybody here who's have to be here right now who's in the ROE business?

MR. MAKHOLM: Dr. Makholm.

MR. HEMPLING: How are you doing? Welcome.

You're going to be here next for the ROE panel?

MR. MAKHOLM: No.

MR. HEMPLING: But you're here now for this panel?

MR. MAKHOLM: Yes.

MR. HEMPLING: Are you familiar with Mr. Parcell's testimony?

MR. MAKHOLM: I don't know.

MR. WILLIAMS: He's not familiar about that testimony.

MR. MAKHOLM: I'm not familiar with that testimony.

MR. HEMPLING: I'm sorry, excuse me one second. Excuse me one second, please.

COMMISSIONER KONDO: Mr. Brosch, may I ask you a question about -- the Commission in its interim had denied the Company's request to implement an RBA. Right?

MR. BROSCH: Yes.

COMMISSIONER KONDO: So if the Commission approves the decoupling as part of its final rate case order, how does the Company implement that given that there's no RBA rate?

MR. BROSCH: My expectation is the Company would make entries on its books to develop the accumulative RBA balance that would then be recoverable through that process in the future by reconciling and comparing the authorized revenues to the actual revenues for the RBA period you would be approving.

COMMISSIONER KONDO: Do you guys have a comment on what your -- or what your thought is and how that would work, is that similar to what Mr. Brosch --

MR. HEE: Could you ask the question again, Commissioner.

COMMISSIONER KONDO: I was curious as to how the

Company would implement decoupling assuming that the Commission approves decoupling as part of this rate case given that the Commission's interim order had denied the Company's request to establish an RBA.

MR. HEE: Commissioner, the mechanism for implementing the sales decoupling or RBA mechanism was identified in the decoupling docket, but I can go over that again.

The implementation would be that we would institute the RBA immediately upon the approval by the Commission; and, if it is before the end of the year, that RBA would be picking up the difference between the target base revenue less those expenses that are tracked either by the ECAC or other tracking mechanisms and the recorded revenue less those same expenses.

COMMISSIONER KONDO: Is that on a forward-going basis?

It's not historic or is it historic?

MR. HEE: That would be on a forward-going basis.

COMMISSIONER KONDO: Okay.

MR. HEE: And speaking of a forward-going basis, even though sales accumulated to date are minus 1.9 percent, because sales currently are approaching the September 2008 test-year sales forecast for the remaining months, it appears that that RBA may not be very large because, as I've indicated, it would be on a forward-going basis.

COMMISSIONER KONDO: All right.

MR. HEE: So, again, to continue, we would, at the end of the year 2009, look at the balance, cumulative balance of the RBA and make a filing in large on March 31st that would include that balance.

COMMISSIONER KONDO: Mr. Hee, I don't mean to interrupt you --

MR. HEE: Okay.

COMMISSIONER KONDO: -- but I understood how it worked. I was just curious --

MR. HEE: Oh, okay.

COMMISSIONER KONDO: -- as to whether the RBA would be established going forward or whether or not it would try to look at what has happened since the interim; but, I think, you answered that question. It's going forward.

MR. HEE: If the Commission felt it should go backwards, of course, we would follow that order.

(Laughter.)

COMMISSIONER KONDO: Is that welcomed here?

Thank you. I understand that.

MR. HEMPLING: I assume there's nobody here who feels that they need to talk about ROE today on the grounds that they won't be here when the chance comes next week. That's a CYA question but I'm required to ask it.

Nobody? Everybody is okay with our, as-planned, having all the ROE questions next week?

I won't be here. You'll be a big crowd.

Before we move on to the ECAC questions, I'm going to suggest that it would useful to the Commission for the parties to consider the various scenarios related procedurally relating to the interaction among the two proceedings.

I don't know if this is an expert witness issue or a lawyer's issue, but it will helpful to the Commission just as, I think, Commissioner Kondo was describing for the Commission to understand the parties preferences as to the sequence of the orders.

Do the parties prefer -- I know the Company would like to get its rate case money as soon as possible, but just to explain to the Commission people's preferences of why for whether the decoupling order should precede the rate case order or vice versa or simultaneously; and, if nobody cares, that'll be useful for the Commission also.

Is that comment clear to everybody?

Is there anything anybody would like to speak to on that topic right now or would you like to save it for the closing statements or the briefs?

Mr. Williams?

MR. WILLIAMS: No, I just think there are a number of possibilities that the Commission could enter an interim decision in the decoupling docket, for example.

I mean, Commissioner Kondo asked an interesting question. What's the effective date, for example, of an RBA; and, then what would the effective date be for the RAM? It would be good to have a decision in place that allowed the RAM to be effective as of the beginning of the year even though -- but you need that order, at least, by sometime before the filing would be due in 2010; and, the RBA, it can either be -- the furthest it could go back would be the date of the interim order; or, it could be made effective by the Commission as of the date of that order, so there are those possibilities and we can address those.

MR. HEMPLING: It's up to the Commission to order this kind of thing; but, I would assume it would be helpful for the Commission to have the best ideas for how to go about managing the two dockets.

MR. WILLIAMS: And that would be -- it's conceivable that it would be helpful as far as the files that are in the decoupling docket by a motion to help address those issues.

MR. HEMPLING: You might want to take into account that it's less work for the Commission to write one order per proceeding than two. I know the advantages of interims, but if it means people have to do work twice, it's just something take into account. Just like you don't want to have to come to the same hearing twice.

MR. WILLIAMS: Okay.

MR. HEMPLING: Anything else on this discussion of decoupling before we move to ECAC?

COMMISSIONER KONDO: Mr. Williams, even your comment --

MR. WILLIAMS: Yes.

COMMISSIONER KONDO: -- about the RAM being in place before the end of the calendar year, I understand that, but, from your perspective, would there be a problem to I want to say retroactively allow -- I guess what I'm trying to say is if the Commission decided decoupling after and the next year in 2010, is there a problem with the Commission going back and retroactively allowing the Company to calculate the RAM as of December 31, 2009, so -- because I understand your comment to be to implement the RAM, the Commission must have a decision before the end of the year?

MR. WILLIAMS: I think the Commission can allow a prospective increase based on the RAM and use a RAM period that goes back to the beginning -- I mean, the end of 2009; but, the real answer to your question is, yes, but it's a -- it turns into a prospective order. You just have a measurement period that affects that. It's just the closer -- the further in to 2010 you get and the more you have to bunch in the recovery.

COMMISSIONER KONDO: I understand. Thank you.

MR. HEMPLING: Okay. I'm going to turn the questions on ECAC now.

For the purpose of these next set of questions is to help the Commission to determine whether the ECAC, as proposed, is consistent with Section 1 of Act 162, so we're going to work our way through the various standards set forth in that statute.

Is everybody with me?

Welcome, Dr. Makholm.

Dr. Makholm, is this your area?

MR. MAKHOLM: In this case, yes, it is. Thank you.

MR. HEMPLING: And thanks for being here.

Now are you familiar with the arguments made by some that a problem with the ECAC is that it relieves the utility of oil price risk changes and that if the utility were exposed to those risk changes, they would have -- the utility would have a greater incentive to reduce its use of oil and to thereby increase its use of renewables?

Are you familiar with that argument?

MR. MAKHOLM: That's a complexed one. Perhaps, we can parse that out.

MR. HEMPLING: I just want to make sure you're familiar with it first.

MR. MAKHOLM: It sounds like a collection of argument.

MR. HEMPLING: Well, what do you think of it?

MR. MAKHOLM: Although, I'll put it into a single sentence.

Perhaps, the first one is whether or not being exposed to oil prices on its own account would compel the Company to purchase fuels it needs for its generated (inaudible) in any way differently than it does if it's not exposed to those oil prices. Maybe we can deal with that one first because that's big and I hear that from time to time in various jurisdictions.

Given the market for oil, HECO is a tiny player, with the amount of oil crossing the ocean and the amount of oil consumed and produced, the tiniest of HECO, as a participant in that market, makes it a price taker; and as a price taker, just like it's a price taker in the market for labor or trucks or vehicles, relatively straightforward processes can allow the Company to demonstrate to the Commission that it's prudent in buying in that market.

Price recovery is easy in the oil market, and it's readily, if the Company has the ready ability to show the Commission and others that it is doing a good job as a price taker in producing from that market.

So the first issue is whether or not being exposed on its own dime to fuel price changes makes the Company act in a different manner, my answer is no.

MR. HEMPLING: The argument that I cited has less to do with the Company making purchases with respect to the generation it currently owns in where to deal with the Company's mix of generation ownership and its incentives to shift the power plant configuration that it relies on from oil to renewables.

So what do you think the argument that if the Company were exposed and had to bear the risks of oil price changes it would be quicker to retire its fossil plans and replace them with renewable purchases?

MR. MAKHOLM: Well, I think this partly gets into Mr. Hee's area, and I'll pass this to him in a second; but, I have often seen arguments that plants that marginally may be more efficient, for instance, in the whole southwestern part of the mainland, there are large, gas-fired plants that as the margin are very deficient in their use of fuels.

MR. HEMPLING: I'm sorry, they're what, sir?

MR. MAKHOLM: Deficient in their use of gas. And some may say that old coal or oil plants that are less efficient in the use of the fuel should be retired in favor of those new plants that are efficient in the use of fuel.

HECO has a larger view of the costs for its ratepayers than that however, as do the utilities in the South, partly in the southeastern part of the U.S., who view this type of argument, because they look out for the totality of the costs of generating to serve their customers.

And it's often the case that older plants, even though marginally they may be less efficient in their use fuel, are far less costly to operate for ratepayers than new plants.

But there's another issue here and this is why I'd like to turn to Mr. Hee. The Company has built into its ECAC an incentive based around heat rate, and that incentive is something that is under discussion with respect to decoupling; and, that's his area, I think, in this proceeding and not mine.

MR. HEMPLING: Yeah. Although, I'm not -- I wonder if we're communicating, gentlemen. I'm not asking about heat rate. The argument that's posed is that y'all have built too many oil plants; and, if you had to have borne the oil price risk all these years, maybe you would have been swifter at getting renewable energy, and that diluted incentive to get more renewable energy dilution arising because of the non-exposure to fuel risk is objectionable. That's the argument, Mr. Hee.

Do you have any response to it?

MR. HEE: I've heard that argument and I maintain that that is an erroneous argument.

MR. HEMPLING: Well, just tell us what the errors are.

MR. HEE: First of all, having an energy cost adjustment clause provides to the utility an incentive for renewable energy and let me say and tell you why.

First of all, having an energy cost adjustment clause allows us to include NR rates without waiting for a rate hearing, a rate case hearing, any costs for a purchased energy for purchase power producers that come online between rate cases, that allows us, the utility, the flexibility of adding these kinds of renewable energy resources at any time without waiting for a rate case, of course, with the approval of the Commission.

Furthermore, the Energy Cost Adjustment Clause provides the utility with an ability to maintain its financial integrity, and it allows these purchase power developers to use the utility as a financially healthy and creditworthy all-taker for the energy that they plan to sell. They can take that information to their financial backers and to the banks and will be able to include or get their projects approved much more completely because of the creditworthiness of the utility. There are other ways that we are incented to add renewable energy exclusive of the Energy Cost Adjustment Clause and those include the renewable portfolio standard.

MR. HEMPLING: Okay. Hold on, Mr. Hee. I'm feeling like I'm hearing something I've heard before.

MR. HEE: Okay.

MR. HEMPLING: Are you sure you're answering the question?

Maybe I'll rephrase it this way.

If the ECAC were amended so that it allowed the purchase -- so that it continued to allow to pass-through your renewable energy purchases but prohibited the automatic pass-through of your oil price costs, if that were the amendment to the ECAC, would the Company be quicker to implement the renewable energy and less quick to build fossil plants?

Would it make a difference?

It's just a hypothetical. Nobody is talking about doing it.

Well, let me start with Mr. Hee because he's the one who was using an old argument for what I think is a new question.

MR. HEE: I think what's going to happen if that were to be the case is that we would have very little opportunity, as a financially sound utility, to do any of the things that argument implies; that even before we would be able to switch to renewable energy, our utility would be in such a financial disarray that we would have no opportunity to make those kinds of decisions that are implied in that question.

MR. HEMPLING: Is this your point, the status quo is what it is. The status quo is you have a lot of oil fire plants, and if you want to remain an economically viable Company, you're going to have to get pass-through the oil costs; and, if you don't, you're not going to be able to do much renewable energy, is that what you're saying?

MR. HEE: It's absolutely true that the ECAC is a key component of our financial health.

MR. HEMPLING: Because of current dependence on oil fire plants?

MR. HEE: Because of our need to pass-through to customers the costs of oil that we procure on their behalf in order to provide them with the electricity that they obviously need.

MR. HEMPLING: What you're saying is the status quo is what it is and it's not going to be changeable by changing the ECAC or what you need now is a strong utility to change the mix by taking on these contractual obligations that, in turn, cause, radiate and cease to wonder and then hope for a quick recovery of fuel costs from the ECAC; is that right?

MR. HEE: What we need is a strong --

MR. HEMPLING: Is that right? Is that correct?

MR. HEE: Yes.

MR. HEMPLING: Thanks, Mr. Williams, but don't coach him much more. It'll make the record unhelpful. At least don't coach him in a direction that's not helpful to the question.

(Laughter.)

MR. HEMPLING: Anything else, Mr. Hee, or do you want to quit while you're still ahead?

MR. HEE: I don't have anything else.

MR. HEMPLING: Dr. Makholm, are you okay with where we are or do you need to hit something of value now?

MR. MAKHOLM: I'd empathize with what Mr. Hee said about maintaining the credit of the Company.

MR. HEMPLING: All right. He said that.

MR. MAKHOLM: The Company does what it does, and the market knows it's necessary for the Company to have prudent pass-through of these costs in order to maintain its credits. It's not just the Company's perspective. That's the perspective that's evaluated by the market.

If the market doesn't believe the Company is creditworthy, it can't be a counter-party for the kind of investments in renewable energy that this Commission in this State seems to want.

MR. HEMPLING: All right.

Sir?

MR. BROSCH: I just want to make sure I understand your question, because I think there's another point that's part of it. If there were no ECAC tracking changes in fuel costs, then rate cases take on a whole new dimension, and we're all about the business of needing to quantify accurately representative fuel prices to bake in the base rates; and, that exercise would be extremely challenging given the volatility in those prices.

MR. HEMPLING: Thank you.

Let's turn to a second question -- second area under ECAC and that's ECAC and risk mitigation techniques.

Mr. Brosch, are you familiar with hedging practices?

MR. BROSCH: I don't have any personal experience. My familiarity is just in working with proceedings like this where it's been discussed.

MR. HEMPLING: All right. So the record is complete, I'm going to quote now Section III of Act 162, which includes, as one of the requirements, that the Commission should, "Allow the public utility to mitigate the risk of sudden or frequent fuel cost changes that cannot otherwise reasonably be mitigated to other commercially available means, such as through fuel hedging contracts."

What's your understanding, Mr. Brosch, of the purpose of financial hedging in the context of fuel costs purchases?

MR. BROSCH: My understanding is that some utilities use financial instruments to hedge their exposure to fuel price changes in the marketplace by trying to take positions that in financial instruments that would move in opposite direction from their physical exposure to those changes.

MR. HEMPLING: Now would these be utilities that have fuel adjustment clauses?

MR. BROSCH: I've seen it used by utilities that do not have fuel adjustment clauses and using both financial instruments as well as physical forward contracts to moderate fuel price exposure.

MR. HEMPLING: Have you seen it in the context of utilities that have fuel adjustment clauses?

MR. BROSCH: Probably, but I don't recall particulars.

MR. HEMPLING: Purchasing a hedge is a cost to the Company. Right?

MR. BROSCH: Yes.

MR. HEMPLING: And it's a price that you pay in order to reduce the risk of high prices?

MR. BROSCH: There is a premium involved in acquiring price stability through hedging instruments, yes.

MR. HEMPLING: So are there some context in which it is prudent and, therefore, recoverable costs to incur a hedging cost if it protects the customers from volatility?

MR. BROSCH: I have observed regulator decisions finding it reasonable to incur additional costs to achieve price stability and fuels and other commodities.

MR. HEMPLING: So the premise of those decisions would be that the customer is better off bearing the hedging costs than the customer would be if there were no hedging?

MR. BROSCH: It must be, yes, sir.

MR. HEMPLING: Do you have an opinion as to whether that is always true, sometimes true, never true, or depends on the facts?

MR. BROSCH: I'm sure it depends on the facts, and I wasn't personally involved in the proceedings, I try to disclaim some responsibility early on in being a student of the decision and the discussion rather than personally involved in the transactions.

MR. HEMPLING: Do you think there ought to be a difference between utilities that have fuel adjustment clauses and utilities that don't in terms of the extent to which they employ financial hedging practices?

MR. BROSCH: I'm not sure. I haven't thought that all the way through. I think, from my experience, the utilities that had more exposure because of the absence of fuel adjustment clause have made their decisions to hedge that exposure for business reasons. You know, and, clearly, if regulators in a fuel adjustment clause environment are supportive of that action and make that known to the utility, I think it would likely be received by the utility as long as the cost of doing so were deemed recoverable.

MR. HEMPLING: Mr. Hee, is this your area, hedging?

MR. HEE: I'm going to pass this to Mr. Alm.

MR. HEMPLING: Well, before you do that, he's your outside consultant, he's not the internal person that makes decisions about incurring fuel costs. Correct?

MR. HEE: That is correct.

MR. HEMPLING: Okay. What's the Company's practice in terms of financial hedging?

MR. HEE: We do not currently financially hedge our fuel purchases. We do have a long-term contract for the purchase of fuel. I am not that witness. It is not a fixed price contract, and we addressed that in the PUC IR 133.

MR. HEMPLING: You addressed what in 133?

MR. HEE: The fact that although we have long-term fuel price contracts those contracts are not fixed price contracts.

MR. HEMPLING: I'm looking at this sum of your various -- sticking with Mr. Hee -- the sum of your various -- the Company's various IRs in this area of 132, 133, 134.

Does the sum of these comments indicate a view of the Company that hedging is a bad thing, it's not economic, it's not good for the ratepayers, is that a misreading of these submissions?

MR. HEE: Yeah, our belief is that there's oftentimes an allure of fuel price hedging and the allure is a fact that perhaps as a result of hedging fuel prices that somehow or other the cost may be lower, perhaps, or at least we would get some kind of a reduction in the volatility; and, while, to some degree, may be true, there are many other risks involved in fuel price hedging that have not come to light other than some of the items that we have filed as documents in this case.

Yes, the fuel price hedging is supposedly going to result in less fuel price risks; but, along with price hedge comes additional risks, which are identified in HECO 1040. That HECO 1040 is an exhibit that was developed by NERA, our consultant, and describes fuel price hedging, and additional risks have come along with it.

MR. HEMPLING: Right. The Commission is familiar with those things.

But is this a concrete inflexible policy on the Company's part that it will never engage in hedging because it's always a bad thing?

I'm not following you.

Is that what you have as a policy against hedging within the Company?

MR. HEE: It's not a policy against hedging. It's in the evaluation of price hedging. As we are discussing it in this rate case proceeding, we do not believe that hedging is the right thing from a standpoint of ratepayers --

MR. HEMPLING: Because the --

MR. HEE: -- because we believe that the costs that ratepayers will eventual pay under a fuel price hedging regime is going to be higher than the prices that they are currently paying now. And I can't -- it has to be clear that you don't enter into a price hedge without paying someone to take the risk and that taking a risk by a third party is going to cost the ratepayers more.

MR. HEMPLING: That's clear.

But is this a generic view about hedging in general or is there something about that HECO-specific facts that has led you personally to this conclusion?

MR. HEE: I think, for that, maybe we need to get into some of the -- my understanding of some of the risks that are involved in fuel price hedging.

For, one thing, it's my understanding that the low sulfur fuel that we purchased here in Hawaiian Electric Company is not a fuel for which a financial forward contract is available for the type of fuel, as well as for the location at which it's delivered; and, as a result of that, there is not easily a forward contract that we can purchase for that exact fuel and for that exact delivery location.

Therefore, a financial hedge, if there was one to be found, would have to be built upon an index that is not exactly the same as the fuel that we purchase; meaning, very likely, that the price movements for that -- I'm going to call it a derivative -- is not going to exactly move along in the same direction as the price of the fuel that we pay. There will always be the difference between those two prices.

And who is taking that risk? That risk can sometimes be large; and, so that amount of risk is that basis risk to which the Company, as well as ratepayers, would be subject, which doesn't exist now.

MR. HEMPLING: What you're saying is, because I asked you about HECO specifically so that you're not in a position of saying that hedging is never a good idea, you're saying that with respect to the particular type of fuel on which HECO's generators are dependent is such that the costs that you incur to buy the hedge is not going to be matched by sufficient benefits to make it worthwhile because there's still going to be substantial price risks even after you pay for the hedge, is that a fair summary?

MR. HEE: Yes.

MR. HEMPLING: And that's a HECO-specific analysis that you've done?

MR. HEE: That is a HECO-specific analysis, yes.

MR. HEMPLING: And is there anything about the facts surrounding most low sulfur fuel that were they to change that the Company's analysis would change?

MR. HEE: I suppose that's possible. As I've said, I'm not the witness on how those contracts and indices are developed.

MR. HEMPLING: Now give me a second, please.

So, Dr. Makholm, you've not advised the Company that hedging is never a prudent practice, have you?

MR. MAKHOLM: I've advised the Company that hedging, which is the new kid on the block for American utilities, no one hedged fuel prices 20 years ago, hedging and use of derivatives for utilities is as modern as the use of derivatives for credit default swaps, and it's to ask -- to put the question a little bit differently, is there a reason for the Company to engage in this new practice?

And, I have advised the Company that given the various downsize, which are that, it's very costly, both in administrative, and in terms that in the amount of money that's paid to counter-parties like Goldman Sachs, who's the biggest counter-party in hedge funds through their subsidiary called J. Herring, given that it's only short-term, hedging markets beyond about 12 to 18 months are very illiquid and as the price goes up hugely and you get on beyond that.

Given that, those apply to any utilities. For HECO, the hedge would have to be imperfect. It's not like HECO is in Oklahoma sitting on the Henry Hub where it knows the gas prices in nine minutes, as a very liquid market right there in the Henry Hub. You're in the middle of the Pacific Ocean, and the ability to buy hedge products that match this Company's needs don't exist in a liquid market.

Given those items, some of which, but all utilities and some of which is specifically applicable to HECO, I've advised the Company that there's no countervailing benefit for customers to deal with the costs, the imperfect nature of the hedge, the short-term nature of this business, it would make it a worthwhile policy for the Company to pursue it on the ratepayers we have.

MR. HEMPLING: And so you don't think the Company's protected from all volatility as the result of the current operation of ECAC enters into their decision not to hedge. These are generic, both generic in HECO's specific advice you're getting -- your giving in terms of the cost benefit analysis of hedging at this time?

MR. MAKHOLM: But it's not the Company's money. It's the ratepayers money that they're looking out for in the decision not to go down this path.

MR. HEMPLING: Dr. Makholm, what about physical hedging? What I'm really referring to is long-term fuel contracts, are you familiar with the Company's contracting practices in terms of the length of time that they commit?

MR. MAKHOLM: Generally, yes, they're not too different from what I'm familiar with generally for American utilities.

MR. HEMPLING: They're not different in what respect, in terms of the mix of long-, short-, median-term?

MR. MAKHOLM: It's different in terms of the history of how electric utilities in America bought fuel. Twenty years, ago long-term contracts fixed prices were common for all American utilities. Gas was a regulated commodity in the U.S. Thirty years ago, oil was a regulated commodity in the U.S. and it was common to find companies that would sell long-term contracts for fixed priced oil gas.

We now have much more highly liquid worldwide markets in oil, and we have American -- North American liquid market in gas and, hence, the types of long-term fixed price contracts that American utilities used to rely upon are gone.

As Mr. Hee said, the Company has long-term contracts but the price terms move unlike the price terms it would have been unlikely seen 20 years ago.

MR. HEMPLING: So they have long-term security of supply but the prices are still going to vary?

MR. MAKHOLM: That's correct. That's very much like if you ask contracts for utilities in the other 48 states, many them are long-term contracts, all the pricing terms are indexed to some market price.

MR. HEMPLING: Gentlemen, from the Consumer Advocate, anything to add to this conversation about hedging and lack of hedging?

MR. BROSCH: No, nothing.

COMMISSIONER KONDO: I don't want to repeat the argument that we had during the decoupling proceeding, so I just want confirmation from the parties that assuming the Commission implements the decoupling mechanism, as part of this rate case, that the positions of the parties that would have articulated both orally as well as in writing relating to ECAC adjustments that those do not require any further discussion or modification; and, if there is, I'd like to discuss that now, because I'm assuming that the Commission will take administrative notice, or whatever the correct term is, of the filings in the decoupling docket relating to ECAC.

Do you guys have anything to add on that?

I'll go with you guys first, if you want, Consumer Advocate.

Do you want to add anything to that, because you talked about the pass-through?

Is there anything new that you want to add to that discussion?

MR. HERZ: No.

COMMISSIONER KONDO: Thank you.

How about from the Company's position?

MR. WILLIAMS: None.

COMMISSIONER KONDO: I know that the DOD was not part of that docket.

Do you have any issue with us taking administrative notice of those discussions and filings, and if the Commission approves the decoupling mechanism, that the Commission will rely upon that discussion in that docket to implement an appropriate ECAC, if it so chooses?

MR. MCCORMICK: We have no objection to that approach.

COMMISSIONER KONDO: Okay. Thank you.

I don't have anything further.

MR. WILLIAMS: Just for the record, since we need to need to do this by counsel, as well, we don't have an objection as well.

COMMISSIONER KONDO: I thought the Company was good enough; but, thank you.

And I assume that if it's got to be by counsel that the CA is okay with it too?

MR. ITOMURA: Yes, the CA has no objections.

COMMISSIONER KONDO: Thank you.

CHAIRMAN CALIBOSO: This completes the panel of the sales decoupling and ECAC.

So I'd like to give the parties a chance to cross-examine each other, if you so choose?

Mr. Williams, would you like to start?

MR. WILLIAMS: If I can just take ten seconds here.

I'm not --

CHAIRMAN CALIBOSO: Sure.

And we'll probably break for lunch early, and you may want to think about the next two or three panels, if you can get your witnesses available, because even tomorrow's panel, the first panel in the morning, you might be able to get to it this afternoon, if your witnesses are available.

MR. WILLIAMS: I don't have any further questions.

CHAIRMAN CALIBOSO: Thank you, Mr. Williams.

Mr. Itomura?

MR. ITOMURA: The Consumer Advocate has no questions.

CHAIRMAN CALIBOSO: Mr. McCormick?

MR. MCCORMICK: The Department of Defense has nothing further.

CHAIRMAN CALIBOSO: All right. We'll try to address both panels, seven and eight, this afternoon.

We'll take our normal, hour-and-a-half break. Let's take a little longer and come back at 1:15, if that's okay with everyone.

Okay. We are in recess. Thank you.

(Whereupon, at 11:34 a.m., a recess was taken, and the proceedings resumed at 1:16 p.m., this same day.)

A F T E R N O O N   P R O C E E D I N G S

CHAIRMAN CALIBOSO: Good afternoon.

This hearing is reconvened.

We are continuing with this panel hearing and starting on Panel 7, which is Purchased Power Adjustment Clause.

Can we have the parties' witnesses?

MR. WILLIAMS: Good afternoon, Mr. Chairman.

The witnesses for Hawaiian Electric for this panel are Tayne Sekimura and Peter Young, both have been sworn in.

CHAIRMAN CALIBOSO: Thank you.

MR. ITOMURA: Good afternoon, Chair Caliboso, Commissioner Cole, Commissioner Kondo.

Our witnesses for this panel will be Mike Brosch, Joe Herz; and, also including Steve Carver.

MR. MCCORMICK: The Department of Defense will have no witnesses.

CHAIRMAN CALIBOSO: Thank you, everyone.

Mr. Hempling?

MR. HEMPLING: This panel is going to focus on the Purchase Power Adjustment Clause.

Could we start by getting a clearer description of what goes into the Purchase Power Adjustment Clause and what does not?

Who's got this over here, is it Mr. Herz or

Mr. Brosch?

MR. BROSCH: Depending on the questions, either one of us. I'll start.

MR. HEMPLING: Is this primarily, Mr. Young?

MR. WILLIAMS: Mr. Young.

MR. HEMPLING: Okay. Mr. Young, let's start with you okay.

MR. YOUNG: Yes.

MR. HEMPLING: Existing PPAs, how would they be recovered under your proposal?

MR. YOUNG: For the existing Purchase Power Agreements, currently, energy payments are recovered both in base rates and in the purchase power -- I'm sorry, in the Energy Cost Adjustment Clause.

This proposal asks that all nonenergy payments, the payments to purchase power providers that are not in base rates -- I'm sorry, that are not in the Energy Cost Adjustment Clause and payments.

MR. HEMPLING: Give you a second. Say this again, will you?

MR. YOUNG: Thank you.

MR. HEMPLING: With respect to these existing PPAs, all costs, other than the energy costs --

MR. YOUNG: With respect to existing purchase powered -- purchase power units all costs, other than the energy payments, would be included in this clause. That would include capacity payments as well as payments for fixed O&M obligations under those contracts.

MR. HEMPLING: With respect to the proposed Purchase Power Adjustment Clause, would you be taking all nonenergy costs out of base rates and putting it into the PPAC?

MR. YOUNG: Yes, that is our proposal.

MR. HEMPLING: Okay. So there would be -- and the same treatment would apply to new PPAs.

MR. YOUNG: Yes.

MR. HEMPLING: So there would be no base rate recovery of anything relating to PPAs under your proposal?

MR. YOUNG: There would still be base rate recovery of energy payments related to purchase power contracts.

MR. HEMPLING: To the extent those energy payments are not being recovered through the ECAC?

MR. YOUNG: Yes.

MR. HEMPLING: What's the reason for leaving some energy payments, some energy costs on base rates but none of the nonenergy costs in base rates?

MR. YOUNG: It has to do with how we set up our base rates and then set up our Energy Cost Adjustment Clause. Our base rates are set up, in our rate case, based on certain assumptions for fuel costs and purchased energy costs; and, our base rates are set based on those costs; and, to the extent that there is variation that we can -- are allowed to recover or refund through the Energy Cost Adjustment Clause, that clause reflects those adjustments.

MR. HEMPLING: Okay. Thank you.

Still in terms of understanding how all this works, tell us about the interaction between the proposed PPAC and purchases the Company will make under fee and tariffs, how will purchases made under fee and tariffs to be recovered?

MR. YOUNG: My understanding is it would depend on the nature of the payments under the fee and tariffs, if the payments under the fee and tariffs are for purchased energy only, the intent would be to recover them, if it's, let's say, the payment is initially after base rates are established, we would recover those costs through the Energy Cost Adjustment Clause; and, at some future point, the payment would be reflected in base rates.

MR. HEMPLING: Run that by me again, please.

MR. YOUNG: If the payment -- if the fee and tariff payment is for purchased energy only, the costs would be recovered through the Energy Cost Adjustment Clause and at some future date it might be reflected in base rates.

MR. HEMPLING: Since --

MR. YOUNG: That's with other purchase power energy payments.

MR. HEMPLING: All right. And if fee and tariff is recovering costs other than energy-only costs, then what?

MR. YOUNG: Then we would intend to include it in the recovery of purchased power costs in the Purchase Power Adjustment Clause.

MR. HEMPLING: Do we know yet how the Company is going to design these fee and tariffs in terms of whether there's going to be a -- well, let me restate that.

Are the payments by the Company to sellers under the fee and tariffs going to be payments that separate compensation for energy from composition for nonenergy costs?

Do you know?

MR. YOUNG: Actually, I don't know. I believe that is still being determined in that docket.

MR. HEMPLING: Well, the order is issued. I guess it's still being determined by the people who are going to file the tariffs for Commission review?

MR. YOUNG: That's my understanding.

MR. HEMPLING: Okay. So if the fee and tariff is designed to compensate the seller for capacity and energy costs on a per-kWh basis, how would the Company -- how would the PPAC, as proposed in this docket, treat those payments?

I mean, let me -- can I explain to you what my potentially wrong understanding of all of this is.

As I understand the purpose of the fee and tariff, is to get the seller on a per-kWh basis an amount of dollars large enough over some period of time so they're willing to make an investment; so, my understanding is that the per=kWh payments from the utility to the seller will, in effect, compensate the seller for its energy and capacity costs without making a specific distinction between the two, is that a possible way in which the tariffs would be designed?

MR. YOUNG: Yes, I believe the tariffs could be designed in that manner.

MR. HEMPLING: Let's just take that as a hypothetical. Under that circumstance, how does your proposed PPAC in this docket charge ratepayers for the payments made by the Company to the fee and tariff seller, everything through the energy clause -- excuse me, everything through the ECAC because it's a per kWh charge?

MR. YOUNG: Certainly, the fee and tariff could design payments to a provider in that manner. For cost recovery purposes, we certainly would want to study and make some analysis of how that might be allocated to both the Energy Cost Adjustment Clause and the Purchase Power Adjustment Clause, if that could be done.

MR. HEMPLING: Okay. Generally, Mr. Herz, I don't know if we're in an area of irrelevancy or not, but do you care, as a matter of policy, one way or the other, as to whether under the assumption that the current kWh payments to fee and tariff sellers are the only payments made, such that they recover, in effect, both energy and nonenergy costs, do you care how the Company allocates those payments between the new PPAC and ECAC?

Does it matter?

MR. HERZ: I think that if the payments are based on a per-kilowatt-hour basis then that should flow through the ECAC, through the purchase energy as to the provision of the ECAC; and, then anything that's nonenergy payment would flow through the PPAC.

MR. HEMPLING: Right, but maybe my question wasn't clear.

What if the payments under the fee and tariff from the utility to the seller are not two-part payments, they're just a single per-kWh charge that's been set high enough so that the seller gets what it needs to pay for its expenses and make money?

What if that's the situation, then what?

Do you care?

MR. HERZ: Well, I think I would care more about how the fee and tariff payment is being structured than the pass-through provision. If the fee and tariff, for whatever reason is structured, that's it's going to be an energy-only payment, then the pass-through should be through, I believe, it should be through the ECAC for the recovery of those energy payments.

MR. HEMPLING: In other words, you don't want the Company to start figuring out, by analysis, how to subdivide a single per-kWh payment to the seller, subdivide that between hypothetical capacity and hypothetical energy costs and then allocating those two between the two recovery devices, one being the PPAC and the other being the ECAC?

MR. HERZ: No, that's correct; not, initially, unless, as we go along and get some experience or something that we learn in the process that would cause us to want to revisit it. Initially, regardless of how the rate was arrived at, whether it's variable and fixed costs, that are to be included in an energy payment, if it's an energy payment, then it would flow through the ECAC calculation.

MR. HEMPLING: So given that there currently is uncertainty about how the Company with Commission approval would design the fee and tariff, is there any need to -- is there any need to address this at this time in the PPAC proposal?

MR. HERZ: I don't think so, no.

MR. HEMPLING: So the Commission should be on the lookout for the issue when the fee and tariff proposes come into the Commission?

MR. HERZ: Yes, I think, that's the better place to deal with it.

MR. HEMPLING: Are you worried about the test year being distorted because we're now allowing -- we would not, under the PPAC, be recovering large payments through faster mechanisms rather than the context of a test year rate case?

MR. HERZ: Normally, from my perspective, I prefer to see capacity payments recovered through base rates. The differences here, though, in why I think it should be those payments should be removed from base rates and recovered through the PPAC is that, one, is that we've got decoupling taking place there and doing this would be consistent with that second --

MR. HEMPLING: Hold on -- just hold on right there. You don't have decoupling taking place yet, you know that?

MR. HERZ: Yes, I understand.

MR. HEMPLING: But now what's the connection?

MR. HERZ: If we -- if we decouple -- if we proceed with some form of decoupling, then the purchase power demand -- the nonenergy related purchase power charges would then -- could they be separated and separately identified from all other costs that are being dealt with through the decoupling in any annual adders that may result from that.

MR. HEMPLING: I'm sorry, I'm not getting it.

We're talking about the potential for having a PPAC -- excuse me, we're talking about the potential for a new PPAC to distort cost recovery because we're focusing on recovering positives and not looking at negatives.

And what are you saying about decoupling that avoids that problem?

MR. HERZ: I think by separating out the purchase power costs from the other utility operating costs, it makes it easier to verify and account for these dollars. The decoupling would, as I understand it, basically involve an annual review; whereas, with the PPAC, it's a matter that is going to basically be a monthly adder with quarterly reviews; and, so I think having these charges pulled out of the base rates allows for that review process to -- makes it easier, I think, for the review process to occur relating to the PPAC.

MR. HEMPLING: I hope I'm the only one in the room not getting this. Let me see if I can come back to it --

MR. HERZ: Okay.

MR. HEMPLING: -- but maybe it'll gel in my mind.

Mr. Brosch -- Mr. Herz, do you want to finish what you're saying?

MR. HERZ: I was going to go to some other reasons --

MR. HEMPLING: Hang on to that. I've got to see --

MR. HERZ: Okay.

MR. HEMPLING: -- if I can understand.

MR. BROSCH: Let me try and see --

MR. HEMPLING: Are you getting it?

CHAIRMAN CALIBOSO: No.

MR. HEMPLING: Okay.

MR. BROSCH: Let me try to add something and see --

MR. HEMPLING: I'm not the only one in the room.

MR. BROSCH: -- if it helps.

I understood your question to be one of other concerns with matching --

MR. HEMPLING: Yes.

MR. BROSCH: -- if we single out the purchase power, what's called a demand cost or piecemeal recovery through a rider, where, historically, they've been collected through base rate.

And I agree, with Mr. Herz, that normally would be problematic. It's problematic conceptually, because in a traditional regulatory environment, you imagine the utility needing to add generating capacity to accommodate load growth and the utility normally, without decoupling, would enjoy some additional margin revenues from load growth that might be available between rate cases to help pay for added capacity; or, said differently, if you make the utility absorb changes in demand charges between test years, then in a next rate case you can match up the sales volumes and margin revenues with the cost of capacity to serve that number of customers and everything else is linked up.

But when you introduce decoupling, the utility no longer has any opportunity to keep for shareholders the margin revenues that historically have arisen from adding customers and sales; so, once you take that away by a decoupling, then you don't have the argument that there's this matching between test years that might cause one to offset the other; and, in that environment, tracking is more tolerable, tracking of purchase power demand charges through a rider.

MR. HEMPLING: So a concern -- really, what you're saying is that a concern with distortion of the test year is an outdated concern in era of decoupling?

MR. BROSCH: If you decouple, then you don't have the argument you would otherwise have that sales growth between test years can help pay for demand charge growth between test years.

MR. HEMPLING: So this is a nice example of how the Commission has to understand the distinction between two -- the relationship between two proceedings, both of which are pending.

MR. BROSCH: I think that's fair, yes.

MR. HEMPLING: And make a decision that's consistent between the two.

MR. BROSCH: I think that's fair; although, I would also observe that the PPAC was provided for in the HCEI agreement, and the Consumer Advocate's support is related to the idea that we want the Company to be indifferent in adding renewable resources and the costs they might bring between test years.

MR. HEMPLING: Well, that's for the Consumer Advocate to worry about, but for you to worry about, as an expert witness, your concern about single-issue ratemaking would return if the Commission did not approve decoupling. Correct?

MR. BROSCH: That argument would be back, yes.

MR. HEMPLING: No, it would be your concern.

MR. BROSCH: It would be and has been, yes, sir.

MR. HEMPLING: Okay.

COMMISSIONER KONDO: Excuse me. If you have no decoupling, Mr. Brosch, but you expect sales growth to decline, do you have that same concern or is it back to the decoupling situation because you don't anticipate having the sales growth to pay for the demanding growth?

MR. BROSCH: I think, at that point, you have different concerns. You probably have utility concerns raised about attrition where the historical opportunity to offset expense growth between test years is gone because of the absence of sales growth.

MR. HEMPLING: Somewhere in this train of discussion, Mr. Herz, I know you were getting to a point number two and point number three.

MR. HERZ: At least point number two.

MR. HEMPLING: Okay. What was the question?

MR. HERZ: The question was why coal purchase demand charges out of the base rates and recover them through a pass-through adder as they occur.

MR. HEMPLING: Okay.

MR. HERZ: And the second reason I was going to get to is that it relates to the interests in adding renewable resources to the system; mostly, through third-parties, and with a pass-through provision, it eliminates the perception that some may have if there's a disincentive for the Company to add these recourses; particularly, those that have purchase power demand charges because they wouldn't be able to recover the costs of adding those until their next -- until those costs could be folded into their base rates.

MR. HEMPLING: So between Mr. Brosch's concern about distortion of the test year, if there's decoupling, and your statement about the PPAC being consistent with a policy of promoting renewable energy, the combination of those two is sufficient for you to be comfortable with PPAC before we get to Ms. Sekimura's concern about that treatment; is that correct?

MR. HERZ: Yes.

MR. HEMPLING: Mr. Herz?

MR. HERZ: Yes.

MR. HEMPLING: Mr. Brosch?

MR. BROSCH: I would say, yes, I would encourage the Commission to put this on the list of issue to consider with return on equity next week.

MR. HEMPLING: This being?

MR. BROSCH: The operational risk shifts brought about this regulatory sweetener of writer recovery of purchase power changes.

MR. HEMPLING: But you're not the ROE expert?

MR. BROSCH: No.

MR. HEMPLING: I just want to make sure it's on our list.

MR. BROSCH: Just on the list. I keep putting it on the list.

MR. HEMPLING: Okay. Because -- okay.

COMMISSIONER KONDO: Mr. Herz, could I follow up with a question?

Your point number two about eliminating the disincentive to the Company to incorporate more renewable energy on your systems, is that a real issue, given that there are other incentives or perhaps disincentives to the Company not to put the energy on the system; and, what I'm talking about specifically under RTS standards, given that they have goals to meet, is there any business incentive for the Company to put renewables on the system that the PPA see (inaudible)?

MR. HERZ: Well, to a certain extent, you know, those standards telling the Company to do so, it certainly helps; but, a lot of renewable resource suggestions in the past, the larger ones could be anticipated by the Company in advance and then planned for and taken into account in conjunction with their next rate case filing; but, as we move to more expedited means of adding renewable resources from third parties, such as a fee and tariff, where the payment and the contract is preapproved by the Commission, I think it's -- I think it's only appropriate in that situation to then allow the Company to recover those costs as they -- as they incur those costs.

So I think in -- I think some may perceive that there'd be a disincentive such as in a fee and tariff to drag through a process -- I'm just using this for an example and I'm not suggesting that anyone would do this -- but drag through the process to not allow or because the transactions to occur later rather than sooner absent a cost recovery mechanism.

COMMISSIONER KONDO: I don't know if you're just using the fee and tariff as an example and there's other examples, but I think I'm getting confused because I thought we talked about fee and tariffs perhaps being recovered through ECAC and not through the PPAC.

MR. HERZ: In the exchange we had, we were looking at energy cost recovery of fee and tariff rates, but I wouldn't be surprised that as we are developing the fee and tariff rates, I think it's likely that most of the transactions were tier one and, perhaps, most for tier two, you know, the 10-kWh and smaller and smaller and then above 10-kWh to the limits. It varies. I could see where giving those size ranges, there are reasons to have an energy-only cost recovery; but, as we get into tier three, where we're dealing with much larger units and perhaps have the opportunity there to provide an incentive for the operator to produce power on demand, I think we may -- I think there could be a good place for a demand energy rate there; and, then it would also encourage or avoid payments that would otherwise would be made if the upon request for performance or the on-peak performance doesn't occur as we would like it to.

COMMISSIONER KONDO: Assuming that to be the case where you have some type of demand charge that for the larger generators, the reason why you believe the PPAC is appropriate is because it's unable -- it's difficult to predict the amount of energy that will be coming through the FIT; is that correct?

MR. HERZ: That's correct. And then you add to that that not only is it difficult to predict, but that the approval process would be preapproved as to approval of each transaction. You know, if we have a standard offer contract versus a more typical PPA agreement where the Consumer

Advocate and the Commission could look at it at the time it becomes available, if we have pre-approval, it seems that what would -- it should go with that is cost recovery of those preapproved contracts.

COMMISSIONER KONDO: Okay. Thank you, Mr. Herz.

MR. HEMPLING: Mr. Young, now what's the reason for taking the existing purchase power agreements which are already in base rates, they're nonenergy costs, and putting them into the PPAC, what's the rationale for that?

MR. YOUNG: I think Ms. Sekimura is better able to speak to that.

MR. HEMPLING: Okay.

Do you understand the question?

MS. SEKIMURA: The rationale for that is the existing purchase power agreements that we have ADS Kalaeola and H Power resulted in imputed debt of 430 million; so, it's very significant in terms of its impact on our credit metrics.

MR. HEMPLING: Okay. So that's a specific reason why the old ones are moving -- you're proposing to move them from base rates is to get the advantage of the reduced imputation of debt?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Which reason is also a reason for putting the new contracts as they come in --

MS. SEKIMURA: That's correct.

MR. HEMPLING: -- under the PPAC.

MS. SEKIMURA: That's correct.

MR. HEMPLING: Can I ask you a question about phraseology to help me?

When the -- so we're now on the rating agency's issue; so, you're on.

This phrase 25 percent risk factor, 50 percent risk factor, what exactly is it?

What's the 25 percent of percentage of?

MS. SEKIMURA: When the rating agencies calculate the imputed debt, they take their present value of the future capacity payment and they multiply it by an average discount rate; and, in this case, they used 6 percent, and then they multiply it by the risk factor and, therefore, a higher -- to come up with imputed debt; so, a higher risk factor will result in a higher imputed debt.

MR. HEMPLING: Do you have any idea why the risk factor isn't down to zero when you take a purchase power obligation and put all of this into a monthly recovery, why is the risk factor anything other than zero?

Do you know?

MS. SEKIMURA: When speaking specifically with the rating agencies of what would result in a zero percent risk factor, they did indicate that it would require legislative action or something guaranteed by law.

MR. HEMPLING: You're referring to what some people call "securitization"?

MS. SEKIMURA: Yes.

MR. HEMPLING: I know this is going to sound like a dunce-cap question, but when we talk about this 25 percent -- excuse me -- risk factor, we're talking about a risk factor that's incremental to the risk factor that normally is applied to Company-owned generation; is that right?

Or let me restate it. I can tell by the look on your face it was not a good question.

When the Company finances its own plan, as opposed to purchase and power, that is viewed as a risk by the rating agencies. Right?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Because part of if you're funding with borrowed capital?

MS. SEKIMURA: That's correct.

MR. HEMPLING: So is what you're saying that if the -- if the risk factor came down to zero for PPA recovery because the legislature passed the securitization statute, would that zero risk factor then make the PPA viewed by Wall Street as less risky than typical utility financed assets?

MS. SEKIMURA: That's correct.

MR. HEMPLING: So where's the equivalence?

At what point in this risk factor analysis is there equivalence between the debt imputation and typical utility finance investment?

Is that question -- can you rephrase that question in a way to make it useful?

MS. SEKIMURA: Well, let me --

MR. HEMPLING: Answer yes.

MS. SEKIMURA: -- restate what I think you said.

MR. HEMPLING: Okay.

MS. SEKIMURA: How do you view Company-owned generation with a purchase power agreement in terms of the risks associated with those types of arrangements?

MR. HEMPLING: That's almost it but I think I'm asking something different. Let me step back for a second.

Some people view this imputation process that rating agencies apply is somehow a penalty on purchase power, and is it the purchase power bears some higher level of risk relative to utility finance asset and that's not exactly correct, right, because there's fully securitized PPAs by statute. There could be fully securitized utility investments and both types of obligations have risks. Right?

MS. SEKIMURA: That's correct. And --

MR. HEMPLING: Oh, wait a minute.

MS. SEKIMURA: -- can I explain the rationale for rating agencies imputing debt is to make an evaluation of the risks that companies undertake. Company-owned generation, we need to go out and secure financing through debt; and, in order to compare what the proxy debt would be for generation that would otherwise be Company-owned, that's the process that rating agencies go through in terms of putting them on equal footing for purposes of analyzing the amount of leverage.

MR. HEMPLING: And that's what this really is about is rating agencies trying to treat -- trying to find a common way to treat risks associated with either contractual obligations of PPAs versus utility financing assets?

MS. SEKIMURA: Yes.

MR. HEMPLING: Are you aware of any -- is there a bias in Wall Street's treatment against these contractual obligations or are they really just trying to find their equivalence to utility financed projects?

MS. SEKIMURA: I don't think there's a bias. I think Wall Street is trying to look for more transparency in terms of the transactions that companies enter into. If you look at pre-Enron, there were a lot of transactions that were involved with purchase power agreements and other types of transactions which were classified as off-balance sheet, and it wasn't necessarily the transparency needed for an investor to make good decisions about how they view companies.

MR. HEMPLING: Don't you find this 25 percent and 50 percent business kind of rough?

They don't sound like they're a particularly fine-tuned analyses of risks; is that correct?

MS. SEKIMURA: I would say that's a good characterization. The other point I wanted to make is if we take a look back in history in terms of how rating agencies have viewed the risks associated with purchase power agreements that back, in 1995, our imputed debt associated with the three existing purchase power agreements was at 175 -- 79 million.

Over the years, they've changed their views and risks associated with purchase power agreements. We didn't change those agreements. It's just the rating agencies views.

Now what they do is they impute a 50-percent risk factor, almost double of what was in place in 1995, such that our imputed debt is now about 430,000,000. In addition to that, they instituted a new mechanism called the Evergreen Treatment, which effective has contracts rolling over a 12-year term; so, it's a constant 12-year term.

And so with the way they have viewed these agreements imputed debt has increased, so, you know, they changed their views as time has gone on.

MR. HEMPLING: So for a given increment of capacity that the Company has to acquire, is it your view that the treatment by Wall Street of utility owned capacity versus purchase power is sufficiently consistent that the Company is indifferent to whether it requires resources through ownership or through purchase or is the Company not indifferent?

MS. SEKIMURA: I would say that the Company needs to look at the alternatives for acquiring new generation and what makes sense from a customer's standpoint in terms of reasonableness of costs need to be considered.

MR. HEMPLING: That's not really a direct answer I'm asking you.

I'm asking you, Looking at the debt imputation process itself and the effect on the Company's balance sheet of either financing its own generation or obligating itself in a PPA, is the Company in a position now, because of Wall Street's treatment to be indifferent between the two options, everything else being equal about the quality of the power and the need and the customer characteristics, et cetera.

MS. SEKIMURA: I would say we're not indifferent. With the debt imputation, we've had to increase the amount of equity percentage in our capital structure and that increases the cost of capital.

MR. HEMPLING: I know that. But have you had to increase it more than you would have if you had financed ownership of the same amount of capacity, everything else being equal, that's exactly what I'm asking?

Excuse me. In other words, if you had to go out and borrow to finance the construction of a new plant, that borrowing would increase the debt on your balance sheet if you had to -- if you wanted to keep the ratios the same, you have to go out and issue more equity. Correct?

MS. SEKIMURA: That's correct.

MR. HEMPLING: All right. So what I'm asking is, given that in either case, either utility ownership or utility purchase under PPA, there is going to be some debt, real debt or imputative debt and there's going to be then commensurately some need to issue more equity. Correct?

MS. SEKIMURA: That's correct.

MR. HEMPLING: And what I'm asking is, As a result of current Wall Street treatment, does the Company find itself indifferent between the two options for acquiring resources or is there, from the Company's perspective, a Wall Street policy that makes it more expensive for the Company to enter into a PPA rather than build its own power supply?

MS. SEKIMURA: I would say over the years it has been more costly with the calculation of imputed debt and because the rating agencies have changed their views of the purchase power agreement, it has become more expensive over the years. There's no certainty in terms of how they would apply a risk factor. It's been changing as opposed to the fixed debt that we take on to finance are large capital projects.

MR. HEMPLING: When you say it's become more expensive, what you're saying is that relative to utility owned -- relative to utility financing of its own projects has become relatively more expensive for the Company to acquire the same capacity through a PPA?

That's what I'm understanding you to say.

MS. SEKIMURA: Yes.

MR. HEMPLING: So that tells me there is a Wall Street bias against purchases under PPAs relative to utility financed assets. That's my interpretation of what you're saying.

Is that a correct interpretation?

MS. SEKIMURA: I would say that Wall Street looks at the recovery mechanism for those costs.

CHAIRMAN CALIBOSO: Ms. Sekimura and Mr. Hempling, let me just jump in.

I thought your previous answer, I heard it differently, I thought you said over time it became more and more expensive to acquire generation with the PPAs over time, not in relation to the utility owned.

Did I hear you correctly?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Okay. Thank for that very important clarification.

So be careful not to agree with me if I'm misstating something. I'm going to try it again. Maybe it's the word "bias" that's disturbing you.

Do you think taking the same amount of capacity for the same purposes clear needs, same quality of capacity, does the Company incur a higher equity cost when it purchases that capacity, as distinct from when it finances it itself?

I assume it's distinct when it finances the same type of asset purchase for its own ownership?

MS. SEKIMURA: I think that we --

MR. HEMPLING: Do you understand my question?

Well, let me try it again. I know it's easier than I'm making it for you, but this is what you're telling me and what Wall Street is saying.

That when you enter into a long-term contract, it's treated as debt, and in order to maintain the capital structure that's comparable to what you had but-for the purchase, you have to pay for more equity. Right?

MS. SEKIMURA: That's correct.

MR. HEMPLING: And if you financed a construction of your own asset, the same asset, with a combination of debt and equity, you have to make sure that you issue enough equity to bear a proper relationship for the new debt. Right?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Okay. What I'm asking you is that in these two situations is the cost to you of having to issue equity higher than the context of the PPA because of Wall Street's treatment; or, for the same asset, is there equivalence to the Company and ultimately to the ratepayer in terms of the transaction, if you know?

MR. WILLIAMS: Just so we have absolute clarity here, are you asking whether there's equivalence with a 50-percent risk imputation factor, a 25-percent imputation factors, because that's what her distinction was before.

MR. HEMPLING: Okay. Thank you.

MR. WILLIAMS: Or are you going to cap a lease which has even imputed factors. I mean, there are differences depending on the structure. I don't know how you take that into account.

MR. HEMPLING: Right. It's, sort of, a three-dimensional --

MR. WILLIAMS: Right.

MR. HEMPLING: -- picture on a two-dimensional -- on a one-dimensional conversation.

Let me put it this way.

What would the Commission policy have to be, the Commission policy or the statutory policy have to be so that there was no equity penalty associated with entering into a PPA as compared to the utility financing the asset for its own purchase, is that framing in the question, Mr. Williams, get your point in?

MR. WILLIAMS: I'll have to leave that to the witness. Yes, I think it does.

MR. HEMPLING: Okay. You were correct to help clarify that, but I wanted to see if I -- does that help at all?

What would the government policy have to be so that Wall Street viewed, as equivalent, a PPA and utility finance asset?

Do you know?

Would it have to be securitization or is it equivalent to the 25 percent or is it equivalent at the 50 percent?

Do you know?

MS. SEKIMURA: I'm not sure I can answer that.

MR. HEMPLING: Because Wall Street hasn't made it clear?

MS. SEKIMURA: I guess I'm still having a problem understanding your question.

MR. HEMPLING: Okay, fair enough. Let me move on. I'll see if I can't make it easier during the break, because I would like the Commission to understand what the incremental cost is to ratepayers of increasing the Company's dependency and purchase power contracts as distinct from utility owned assets.

Okay. That's what I would like us to understand better, and I understand that the equity penalty varies with the clarity and strength of the regulatory promise of cost recovery. Correct?

MS. SEKIMURA: That's correct.

MR. HEMPLING: And we have a range from total ignorance of what the cost recovery will be at one end; meaning, see you in the next rate case versus total certainty in the form of statutory securitization. Correct?

MS. SEKIMURA: That correct.

MR. HEMPLING: Okay. And I think it would be useful for the Company to advise the Commission, at some point, on where in that range of certainty there is equivalence to the Company in terms of financial effect as between a purchase under PPA and a utility finance of an asset. I'm not sure I can make it any clearer than that but, maybe, during the break, you can talk about it with your colleagues.

MS. SEKIMURA: Okay.

MR. HEMPLING: Okay. Thank you for your patience.

Now still sticking with you, and if the gentlemen, if the CA has any thoughts on this, either to help clarify the question or to help answer it, that would be a real contribution.

Now do credit rating -- Ms. Sekimura, do credit rating agencies differentiate in terms of the risk factor they apply between two types of PPAs; one, where the utilities stream of payment obligations is stable and predictable and;

one, where the utilities stream of payment obligations is variable and unknown?

MS. SEKIMURA: Rating agencies have not made that distinction.

MR. HEMPLING: Because their focus is on recoverability?

MS. SEKIMURA: Their focus is on the recoverability, that's correct.

MR. HEMPLING: Certainty of recoverability?

MS. SEKIMURA: Yes.

MR. HEMPLING: The rating agencies are indifferent to the very -- as far as you can tell, the rating agencies are indifferent to the variability of the obligation if the certainty of the recovery is the same?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Mr. Herz, back to the design.

You were involved in the negotiation of the PPAC?

MR. HERZ: I don't recall that -- I don't recall if there was a negotiation because, I think, this was a proposal made by the Company initially and that with the refiling and we reviewed it --

MR. HEMPLING: Okay.

MR. HERZ: -- and --

MR. HEMPLING: You studied it?

MR. HERZ: Yes, studied it, yes.

MR. HEMPLING: Okay. I want to understand, please, this distinction between the monthly recovery and the quarterly adjustments.

Do I have that right?

MR. HERZ: Yes, sir.

MR. HEMPLING: Okay. Do you have any comment on the wisdom of the frequency of those two events?

MR. HERZ: I think that those seem reasonable. There's going to be some estimates involved; and, I think, quarterly is a good time to review and go through a reconciliation process.

MR. HEMPLING: Ms. Sekimura, the monthly would have maximum favorability to the credit rating agencies, because it's as soon as possible --

MS. SEKIMURA: That's correct.

MR. HEMPLING: -- is that correct?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Is that why you folks chose monthly?

MS. SEKIMURA: We chose monthly for that reason, but we also have a quarterly true-up such that the Commission has the opportunity to review those amounts and make adjustments as appropriate.

MR. HEMPLING: Okay. You might want to speak a little louder. I got it, though.

And I don't know if this goes to you or to

Mr. Young, has HECO evaluated how much additional variability in the customer's monthly bills will result in the PPAC, variability in the monthly bills?

MR. YOUNG: This is Mr. Young.

HECO hasn't estimated or tried to project what kind of variability there would be in monthly bills. In our response to PUC IR 128, we did show the history of our nonenergy purchase power expenses from 2006 to 2008, which does indicate that there is some small variability in those expenses, which would be reflected in changing rates under the Purchase Power Adjustment Clause, whether they are monthly or quarterly.

MR. HEMPLING: Basically, we really have no idea what that variability is going to be once we inject the fee and tariffs into the PPAC; is that correct?

No idea?

MR. YOUNG: That would be another factor that we haven't considered.

MR. HEMPLING: Have not considered?

MR. YOUNG: Yeah.

MR. HEMPLING: I shouldn't say no idea. You could make some idea because you have some cap on the volume of purchases that are going to be made under the FIT. Correct?

MR. YOUNG: That's correct.

MR. HEMPLING: Does the Company see any need to look at variability with customers' bills associated with moving to a PPAC?

Any need to do that?

MR. YOUNG: The Company hasn't considered variability as an issue --

MR. HEMPLING: Okay.

MR. YOUNG: -- although, certainly, if variability would -- becomes a concern, there are ways, even within the Purchase Power Adjustment Clause, to, perhaps, deal with that variability.

Let's say, for example, if we start with a quarterly adjustment mechanism, we could increase the frequency to monthly adjustment and that might deal with variability more effectively.

MR. HEMPLING: It's also budget billing for customers that want to select that; is that right?

MR. YOUNG: We currently don't have a budget billing mechanism.

MR. HEMPLING: I'm glad you reminded me of that, because I forgot to ask that question of some witness that I'm afraid might have escaped.

Whose -- did you finish your answer?

MR. YOUNG: Yes.

MR. HEMPLING: Okay. I had this question about budget billing.

As I understand it, the capacity to provide it is connected to the completion of the CIS; is that correct?

Is that not your department, Mr. Young?

MR. YOUNG: Our ability to provide that on a large scale certainly is connected with our CIS that could do that --

MR. HEMPLING: Yeah.

MR. YOUNG: -- which we do not have currently.

MR. HEMPLING: But you're working on it?

MR. YOUNG: Yes.

MR. HEMPLING: You have a little problem with contract of performance with CIS?

MR. YOUNG: I'm not familiar with the details of those issues.

(Laughter.)

MR. HEMPLING: Good answer.

(Laughter.)

MR. HEMPLING: Excuse me one second.

COMMISSIONER KONDO: Can I ask some questions, Mr. Hempling?

MR. HEMPLING: Yes, sir, please.

COMMISSIONER KONDO: I know that the Consumer Advocate had recommended some reporting of the PPAC numbers; is that correct?

MR. HERZ: Yes.

COMMISSIONER KONDO: Could you explain what type of reporting the Consumer Advocate recommended?

MR. HERZ: The reporting would be for the purpose to allow the Consumer Advocate and the Commission to verify that the revenues collected matched to the costs incurred; and, so the reporting would be to identify all of the costs that were eligible for inclusion into the PPAC and any comparison of that with the revenues that were collected through the PPAC adder; and, since all those costs or since none of those costs would be included in the base rates, it should be a relatively straightforward process to make that verification.

COMMISSIONER KONDO: And from your testimony, I got the impression that, in your opinion, the reporting requirement is an important piece of the PPAC puzzle; is that correct?

MR. HERZ: Yes, from the standpoint that if we are having an automatic pass-through tracker, I think it's important for the Consumer Advocate and the Commission to be able to confirm that it's doing what it was intended and only what it was intended to do.

COMMISSIONER KONDO: If the Consumer Advocate and/or the Commission, because of staffing problems, furloughs, or whatever else, is unable to commit the appropriate review to those reporting requirements, would that change your opinion as to the reasonableness of the PPAC?

MR. HERZ: I don't -- no. The answer is no. For the reason that one can -- if one is unable to do it on a quarterly basis, one can always do it on an annual basis or a longer period of time, you could also hire consultants to do it too, but --

(Laughter.)

COMMISSIONER KONDO: Is this your pitch?

(Laughter.)

MR. HEMPLING: Go ahead, Mr. Brosch. I'm sorry.

MR. BROSCH: I was just going to observe that there may be procedures where some sort of -- on a test or even third-party financial review and a test could be appended to those filings and funded by the utility, if that added some comfort. Tools like that have been used in other jurisdictions.

MR. HERZ: But you do bring up a point and that that is one of the concerns; but, adding trackers, there's, undoubtedly, going to be additional administrative matters to deal with, both in the Company, the Consumer Advocate, and the Commission; and, you also have to deal with the fact that it's sometimes difficult to deal with abuses in that you're dealing with the situation where generally the revenue has already been collected.

And now you're doing a retroactive look at that and trying to recover revenues that have already been collected; but, you know, that's just the downside to having trackers.

COMMISSIONER KONDO: I want to, kind of, switch gears a little.

I know in prior Commission dockets where the Company has suggested a PPAC mechanism the Commission and various parties, including the Consumer Advocate had expressed concerns about single-issue ratemaking.

Is that still an issue here or is that issue -- is it no longer single-issue ratemaking because of the reasons that you and Mr. Brosch explained earlier?

Could you enlighten me about that?

MR. BROSCH: Let me answer it this way. I, certainly, had that concept in mind when I was talking about the historical relationship where we have periodic rate cases, everything changes between test years and there was some revenue growth available in most years to help pay for cost changes.

What we have proposed, via decoupling, is an elimination of that risk and opportunity for the utility to experience margin revenue changes between test years; so, you've neutralized that variable in the process.

Then if you look at the RAM proposal that's before you, that has the effect of adjusting between test years on an index basis and on a calculation updating some pieces of rate base to account for fairly holistically the rest of the revenue requirement and how it might be changing between test years; so, once you embrace -- if you embrace that kind of a regime, you really have sort of a global marching update of the revenue requirement and the revenues to meet that revenue requirement taking out of play changes in volumes of business. So piecemeal ratemaking becomes, I would say, less relevant if all of that ends up being approved.

COMMISSIONER KONDO: What happens if the Commission does not approve decoupling, what would be the Consumer Advocate's position on the PPAC?

Does it change because, certainly, if you don't have that scenario that you've just articulated?

MR. HERZ: I think that you should still go forward with the PPAC because of the intention of adding a lot of renewable resources through third parties and provide for the cost recovery as part of achieving that goal.

COMMISSIONER KONDO: Okay. Can you address a single issue, ratemaking issue, then assuming no decoupling?

I understand the reasons why you support the PPAC, but Mr. Brosch explained why it was not a single-issue ratemaking; so, perhaps, that concern is lessened if we have decoupling with the RAM, but I don't understand or, at least, I'm not getting whether that same explanation applies, if we don't have decoupling.

And is it still single-issue ratemaking and is that a concern; and, if not, why not?

MR. HERZ: I think it's -- we'll let Mike Brosch correct me here in a second, but I think it's still -- I think it's still an issue; but, I think that the goal or the policy of trying to reduce dependency on fossil fuels and increase renewable resources has to be considered as well in that it trumps that.

And, in particular, if, as part of this, we are looking at means expediting the procurement process with third parties; and, I think the fee and tariff is a good example that where you have a standard offer of contract that obligates the Company to sign up all takers that meet the eligibility requirements, I think we need to have in place a mechanism that allows the Company to recover the costs of doing so.

COMMISSIONER KONDO: Do I understand what you're saying if I put in the balance single-issue ratemaking on one side and the benefits to allow the Company to incorporate more renewable energy that, in this instance, or under these circumstances, the balance swings in favor of allowing the PPAC and not in favor of the single-issue ratemaking concerns?

Is that what I understand you to be saying?

MR. HERZ: Yes.

COMMISSIONER KONDO: Okay.

MR. BROSCH: And for my part of that, I would say, generically, single-issue ratemaking is undesirable and poor policy absent compelling reasons to practice single-issue ratemaking, and I think that's consistent with Mr. Herz's point.

Normally, regulators, if they have the discretion to adopt or not adopt rate tracking through a writer mechanism for a piece of the revenue requirement would look to criteria like is the cost so large and volatile that the company's financial stability would be jeopardized if it were not tracked; and, what springs to mind there is fuel oil cost for HECO.

What do we want to do with the utility in terms of the incentives that we either create or blunt through a writer recovery mechanism and if you have to evaluate the facts and employee that criteria and ask yourself is it worth it.

Another issue is administrative practicality, and you hit on that a moment ago, can we make the process transparent and simple enough that we'll have some comfort, the resources will be there to monitor it and address any problems that may arise.

These are the kinds of thoughts and arguments that surround departures from traditional test year regulation, and, I think, you have to apply whatever weighing you think is appropriate to those arguments in evaluating a particular proposal.

COMMISSIONER KONDO: Okay. Thank you.

I want to involve Mr. McCormick, if I may, and I'm not sure that -- and you can pass, if you'd like; but, I know that the DOD raised the single-issue ratemaking in this docket as well as prior dockets when the Company had proposed a PPAC.

Can you comment as to the position the DOD has with respect to the PPAC currently?

MR. MCCORMICK: We have no further comment on it. We have made a settlement and thought we resolved those issues as far as further consideration.

COMMISSIONER KONDO: Ms. Sekimura, can I ask you a couple of questions, and Mr. Hempling was getting much more into the detail than I can understand; so, I just want to ask, kind of, a general very broad question.

In the big picture of things, how important to the Company is the PPAC?

I'm trying to get a feel, because there's a lot of mechanisms that we're talking about, and I hear you talking and other people talking how it reduces the risk; so, I'm just trying to get an understanding as to the big picture and the whole equation.

Where does the PPAC fall into a desired mechanism that helps the Company in the eyes of the raters?

MS. SEKIMURA: Okay. Let me point to specifics in terms of where our credit metrics stands and then I'll go into how is this viewed in terms of a rating; so, if I could turn you to the work paper HECO R 2007.

CHAIRMAN CALIBOSO: Do have you the file date for that?

MR. WILLIAMS: It was filed with the rebuttal testimony and I'm not -- I don't recall that exactly.

COMMISSIONER KONDO: All right. Thank you.

MS. SEKIMURA: What this worksheet shows are the financial -- the ratios that the rating agency S&P, in particular, calculate and they take a look at the financial metrics funds from operations to average total of debt. They look at the operations -- funds from operations, interest coverage and total debt to total capital.

What we did on this particular worksheet is to show the impact of a 50 percent risk factor. This is our current state. And a 25 percent risk factor which is with the purchase power adjustment clause.

COMMISSIONER KONDO: Yeah, I'm sorry. I'm not seeing it. It's --

MS. SEKIMURA: Okay. Page --

COMMISSIONER KONDO: Page 1 of 13, HECO RWP 2007?

MS. SEKIMURA: I'm sorry, it's HECO R 2007 page 1 of 1.

COMMISSIONER KONDO: Thank you.

MS. SEKIMURA: I'm sorry. I think I mistakenly identified it as a work paper.

MR. WILLIAMS: There's one and I'll give you another one.

COMMISSIONER KONDO: Okay, thank you.

MS. SEKIMURA: These are the ratios that our rating agencies used to calculate where in the range we fall for credit ratings. We have the calculation at a 50 percent risk factor, which is where we are current state, and we assumed a 25-percent risk factor assuming the PPAC in place.

What you see on the top is the various grades here and the calculation of the ratios for those particular items and where they fall within that particular grade. As an example here, if you take a look at the far right, we have a box there and that is for the total debt to total capital. With the 50-percent risk factor, that ratio is at about 56 percent, and that falls into the non-investment grade double B plus category.

Assuming a Purchase Power Adjustment Clause in place suggestive of a 25 risk-percent factor, that would place that particular metrics in the triple B space; so, there is an improvement there in that particular ratio.

So the point that I wanted to make was with the Purchase Power Adjustment Clause with the reduction in imputed debt it helps us to maintain our credit rating, which is currently at triple B. Currently our metrics our weak for the current triple B rating.

Now how does this relate to the big picture --

COMMISSIONER KONDO: May I ask you a question?

MS. SEKIMURA: Sure.

COMMISSIONER KONDO: You say your metrics are weak.

Does that mean that under this table but-for the fact that the rating agencies are rating you triple B, you would actually fall to BB-plus because that's the box?

MS. SEKIMURA: That is just one of the ratios that they look at.

COMMISSIONER KONDO: And this chart would also say that if the Commission were to grant the requested rate relief but did not grant the PPAC, according to this chart your rating would not move.

Would it still be BB -- plus?

MS. SEKIMURA: Our current rating is triple B. I'm not suggesting that it would necessarily move. Rating agencies also look at other factors. When they're rating our Company, they look at financial metrics, which are quantitative in nature and they also look at qualitative aspects as well. So this is just one consideration.

The point here of this worksheet is you can see that the ratios do improve but they're currently weak to support the current rating.

COMMISSIONER KONDO: If the Commission did not approve the PPAC, do you expect that the Company's rating would be downgraded?

MS. SEKIMURA: I don't know what the rating agencies would do, but imputed debt does have a significant impact on the ratios. I would say that the purpose of the PPAC is to get our metrics, our financial metrics in line with the current rating and with that rating we would be able to promote renewable development.

A lot of the renewables that we see coming in the future are going be in the form of purchase power agreements and, therefore, we would like our ratings to be maintained, our -- these renewable developers, their financing depends on the strength of our Company and our creditworthiness.

COMMISSIONER KONDO: You're talking about the purchase power agreement. You're not talking about the FIT contract. You're talking about other types of negotiated PPA?

MS. SEKIMURA: That's correct.

MR. HEMPLING: Ms. Sekimura, may I interrupt and get clarification there.

Purchases that the Company makes under the fee and tariff are going to be part of obligations that the rating agencies take into account when they're determining imputed debt, yes are no?

MS. SEKIMURA: Yes.

MR. HEMPLING: Okay. I thought you may have said the opposite to the Commissioner.

MS. SEKIMURA: I'm sorry, I misunderstood.

MR. HEMPLING: Okay.

COMMISSIONER KONDO: Thank you.

Okay. I'm sorry, I interrupted you. You were going to tell me about the big picture.

MS. SEKIMURA: So the big picture is a financially sound utility that can maintain investment grade ratings will be able to attract renewable developers whose financing depends largely on our creditworthiness. Much of the renewables that we expect to come online in the future will be done by third parties; and, so the PPA clause, again, will help us to maintain the current financial rating -- current credit rating of a triple B.

COMMISSIONER KONDO: Does that mean that it's very important to the Company that the PPAC be approved?

I'm trying to get an understanding given all the different mechanisms that are on the table.

Is this very important to the Company?

MS. SEKIMURA: I would say it's very important to the Company. It provides with the assurance of the recovery, the strength of the recovery, which the rating agencies need in order to assess a rating for our Company.

COMMISSIONER KONDO: If you can, how does this compare with the REIS that is being proposed in terms of value to the Company?

MS. SEKIMURA: The REIS in addition is a very important part of that picture when we talk about renewables. It allows us, again, to, if approved by the Commission, seek recovery in a timely manner, costs associated integrating renewables.

COMMISSIONER KONDO: More important than the PPAC to the Company, less important, say?

I'm trying to get a feel because there's so many mechanisms, you guys, have thrown to the Commission; so, I'd like to understand in order of importance to the Company which ones are the real important ones.

MS. SEKIMURA: I would say it's equally important --

COMMISSIONER KONDO: Okay.

MS. SEKIMURA: -- in terms of the surcharge and the PPAC, again, to promote the development of renewables in order for us to meet the renewable portfolio standards.

COMMISSIONER KONDO: How much decoupling?

Where does decoupling fall into the importance for the Company versus the PPAC?

More important, less important, the same?

MS. SEKIMURA: I would say it's important for the Company to -- it would be important for the Company.

COMMISSIONER KONDO: I guess I'm asking from the perspective of the market. I know the Company would like it, but I want to know how would it effect the rating?

Is it more important, less important, the same as the PPAC, if you can tell?

MS. SEKIMURA: I would say that currently, because we're in an economic recession, our sales have been on the decline and lower sales has affected our financials and the rating agencies do take careful look in terms of what that does to our financial situation, so it is important.

COMMISSIONER KONDO: More important, less important, the same?

I'm trying to get an understanding as to where things rank.

Are they all important, equally important?

MS. SEKIMURA: I would say that they are all important.

COMMISSIONER KONDO: Okay. Thank you.

CHAIRMAN CALIBOSO: One quick follow-up. It's a lot simpler.

For the Consumer Advocate, you've heard Ms. Sekimura say that for the existing PPAs and the old PPAs to put that into the PPAC, that the benefit is to address the imputed debt issue; and, I understand earlier you said that you're pretty comfortable with PPAC generally.

I just wanted to ask if there's any downside to putting in the existing -- to putting in the existing PPAs into the PPAC.

MR. BROSCH: I'm not aware of any downside. Effectively, you broaden the scope of the adjustment mechanism and attract through this device changes in, for example, the demand charges associated with the existing purchase power agreements; and, in doing so, you've used a specific accounting device for those changes instead of, for instance, applying some more arbitrary inflation rate, like you might in RAM, if you instead included the embedded demand charges from current PPAs in the RAM mechanism.

So from that perspective, you achieve a more direct accounting for those changes, whatever they are; and, I think Mr. Young indicated that historically that's not been a lot of change in those costs between years anyway by reference to the PUC IR he spoke of.

CHAIRMAN CALIBOSO: Thank you.

COMMISSIONER KONDO: I want to ask you about that last statement then and maybe it's Mr. Young's statement that you're talking about.

If there's been no changes, why do we need the PPAC because it's pass-through in base rate?

MR. BROSCH: It depends on whether you look backwards or forwards.

COMMISSIONER KONDO: Okay.

MR. BROSCH: And Mr. Young's analysis looked backwards, and I think Mr. Herz was speaking about the need to provide for changes in the future.

COMMISSIONER KONDO: Okay. No, thank you, I understand that.

I've got another question actually.

When you said there's no downside, isn't the downside whether the tradeoff, the risk that's been shifted, isn't there a downside from the ratepayer perspective?

And, I guess, what I mean by that, because the risk has shifted because there's immediate recovery?

MR. BROSCH: These costs for -- the costs associated with the existing purchase power agreements are recoverable through rates anyway; so, by including them in the tracker that we're talking about, we're specifically accounting for changes in those numbers going forward.

So, the answer to your question was it depends on whether the bogey is continued traditional regulation with RAM or without RAM; and, if it's with RAM, then you have to ask yourself the next question of whether these kinds of costs, if not in a PPAC, would be considered in a RAM escalation environment; and, I haven't considered that because of the PAC.

COMMISSIONER KONDO: All right. Well, thank you.

MR. HEMPLING: Gentlemen, Mr. Herz, Mr. Brosch, I want to try to summarize a few things.

You two fellows have been in this business, Mr. Carver too, for somewhere between 25 and 35 years, most of you working for Consumer Advocates. Correct?

Mr. Brosch?

MR. BROSCH: Consumer Advocates and commission staffs, yes.

MR. HEMPLING: Mr. Herz?

MR. HERZ: Mostly for publicly-owned electric utilities systems and then in with the Consumer Advocate.

MR. HEMPLING: Here's what I'm seeing is the situation, and I'd like to get your comment on it, there are a couple of givens here.

One of the givens is that there's a statutory obligation imposed on the Company to buy a lot of renewable power, correct, in the form of the renewable portfolio standard. Right?

MR. HERZ: Yes.

MR. HEMPLING: A second given is that sales are going down, not just because of the recession, but because it's become the policy of the state to reduce reliance on fossil fuel one way of which is going to be to reduce consumption. Right?

MR. BROSCH: Yes.

MR. HEMPLING: So that's a given. You got a given of an obligation to buy more renewable power and you haven't given declining sales. Correct?

MR. BROSCH: All true, yes; always presently and expected in the future.

MR. HEMPLING: Then from a consumer protection standpoint one is looking for ways to minimize the costs of producing reliable electricity in that context of renewable mandates and a desire to reduce sales. Correct?

MR. BROSCH: I think we're all after the lowest practical cost of reliable service, yes.

MR. HEMPLING: What I'm understanding is that proposals that a Consumer Advocate connected witness would normally be suspicious of quick pass-throughs, guaranteed cost -- virtually guaranteed cost recovery through decoupling, and a multiplicity of surcharges, each one separated by a separate purpose, concepts that Consumer Advocate witnesses would historically be suspicious of, they're favorable toward now because the effect, given the obligations the Company is under, is to reduce costs to the customer, is that the reason why you fellows are not uncomfortable with the series of proposals that the Company is making, such as decoupling, PPAC, and REIS surcharge?

Mr. Brosch?

MR. BROSCH: Well, as I attempted to explain in the decoupling panel, these are extraordinary times calling for extraordinary remedies that are not easily addressed through traditional regulatory tools, and your laundry list of exceptions to traditional regulation are all intended to be responsive to that current environment; and, as we looked at the individual elements of the proposal and collectively at the end result of all of those components, but we see an opportunity for financial stability enhancement for the utility and preservation of its access to capital on reasonable terms which should provide reliability benefits to consumers at the same time we would expect to see consideration given to the -- the call of the effective of all of that on the cost of capital and some shifting of the administrative responsibilities of all the parties involved from an environment that would likely be repetitive, contentious rate cases to deal with all those issues using a form of traditional tools to a replacement of within an environment that with these mechanisms hopefully doesn't involve that kind of contentious crashing about to do back-to-back rate cases.

MR. HEMPLING: Maybe a shorter way for you to answer my question, and I'll try to make it shorter; but, there can be a tendency in proceedings to view the Company and the consumer as at odds and to view proposals that are good for the Company and is bad for their customer, that happens sometimes in proceedings. Right?

MR. BROSCH: It does. We tend to get locked into our advocacy views of the world if we're not careful.

MR. HEMPLING: I'm talking about actual differences in outcomes where what ends up being a proposal and good for the company can turn out to be bad for the customer and that happen sometimes.

MR. BROSCH: Absolutely, there are issues that tend to polarize the parties.

MR. HEMPLING: But you're viewing this situation, decoupling, surcharges, PPACs, as situations where what's good for the Company is good for the ratepayer because it's cost reducing given the mandates and facts that are in the context; is that correct?

MR. BROSCH: Yes, certainly, the desired outcome is a rebalancing of the risk and opportunities and costs, that's correct.

COMMISSIONER KONDO: Mr. Brosch, may I ask you a follow-up question?

You know what I find to be surprisingly absent from your response is the Hawaiian Clean Energy Initiative do you agree with -- is that a factor in that analysis or that response to Mr. Hempling, the CA's agreement for signing off on the HEIC agreement?

MR. BROSCH: Yes, that's certainly a factor that was -- as we -- as I discussed in the decoupling docket with you, that agreement established a framework, a set of tools that we were going to work with and work from to achieve what is recommended to you as a reasonable balanced outcome.

COMMISSIONER KONDO: I understood Mr. Hempling's question to be a question if you back out the HCEI agreement.

Would your response have been the same if the HCEI agreement had not been in place?

MR. BROSCH: I think I answered that question once before too.

COMMISSIONER KONDO: I think you may have, but he asked the question about the CA's support for many of these initiatives that, perhaps, in another setting, you wouldn't have seen the same type of support by the Consumer Advocate's office. And I understood your answer to be because these are extraordinary times, therefore, extraordinary measures are needed; but, from our discussion in the decoupling document, I understood that your starting place was the HCEI agreement; so, in response to Mr. Hempling, I didn't hear that, so that's why I thought maybe the record in this case may not be very clear because your response would indicate to me that it was not a factor in your analysis in your response to Mr. Hempling.

MR. BROSCH: Well, let me try to clarify that.

The starting point here was from the CA's perspective. The framework laid out in the HCEI agreement and the commitments made by the parties to that agreement to work within that framework. From there, the analysis was to, with each of those components, attempt a balancing of consumer interests with the other things I described in my earlier response, a financial stability for the utility preservation of access to capital, administrative practicality, all of those considerations.

Had we in the alternative worked with a clean slate and the challenges presented to the utility and all of us by RPS and the other changes that are envisioned in the agreement, we may have come up with other tools and recommendations for you than the ones you see here.

COMMISSIONER KONDO: Thank you for the clarification.

MR. HEMPLING: I'm sorry, I want to make sure because I asked a slightly different question. I didn't refer to the HCEI agreement at all in this line of questions with you.

I said there's two givens. One is a statutory mandate for the utility to buy a lot of renewable power, and the other is a reality that sales are going to go down.

So what I understand your testimony to be is, given those two facts, which has nothing to do with the Consumer Advocate's political responsibilities but has to do with your speaking as a witness, given those two facts, you're telling the Commission that the PPAC is a cost reducing method for the Company to comply with its mandates.

MR. BROSCH: I'm saying -- well, are we talking about PPAC or all the bundle, one --

MR. HEMPLING: Right now I'm just asking PPAC.

MR. BROSCH: PPAC in isolation, Mr. Herz has looked more at the PPAC in isolation than I have, but I see it as reasonable on its own. It was one of the components prescribed to be considered in the HCEI Agreement and we did consider it for that reason, among others.

MR. HEMPLING: Okay. Ms. Sekimura, I'm wondering whether we can make any more progress on the question that I raised with you; and, if I'm beating a horse that's not going to ride right now, you can tell me that.

There's a -- and I'm referring to this -- I'm referring to my general question of what government policies in Hawaii would be necessary to produce financial equivalence to the Company between a PPA and a utility financed construction of a comparable claim.

Do you remember the outline of conversation we had?

MS. SEKIMURA: Yes.

MR. HEMPLING: Okay. Before we get into any detail, I really want to make sure we understand each other.

I've got this HECO response to PUC IR 131.

Okay. I think, if I've got the same document you have, the last sentence says, "The presence or absence of a PPAC would not directly impact the evaluation of a utility-owned bid. Availability of the clause, referring to PPAC, if it does produce the cost of adding purchase power from third parties, and in that sense, improve their position in the evaluation process vis-a-vis utility-owned generations."

Do you see that?

MS. SEKIMURA: Yes.

MR. HEMPLING: So in the context of a competitive bid, the Company is going to compare two cost defects and we're talking cost defects to the ratepayer of utility-owned generation and a purchase power agreement. Right?

MS. SEKIMURA: That's correct.

MR. HEMPLING: And the existence of the PPAC is going to affect that comparison, that's what you're saying here, because the existence of a PPAC is going to reduce the total costs to the Company because of the reduced imputation of debt. Correct?

MS. SEKIMURA: That's correct.

MR. HEMPLING: But when I asked you -- I'm not trying to be troublesome here, when I asked you what's the government policy that would have to exist in Hawaii to make the utility indifferent between the two; in other words, to "improve their position" so much so that they were seeing as equivalent, your present answer is that you're not sure.

And I don't mean my statement to be accusatory. I just want the record to be clear.

MS. SEKIMURA: Well, I think there's another factor to consider as we look at evaluating and then that's where I'm having difficulty in answering the question.

And that really consists of what type of purchase power agreement, what's the resource fix?

Is it variable as available?

And those factors can't impact how we view comparisons between Company-owned and third-party.

MR. HEMPLING: Well, I think I understand what you're saying.

From Wall Street's perspective, they're strictly focused on this existence of a PPAC or are they also going to vary their debt imputation conclusion based on other details of the contract, such as the ones you've just mentioned.

MS. SEKIMURA: That's correct, they do look at the contract.

Just as a side note, when we take a look at the debt imputation that S&P calculates are as available contracts Wind, in particular, have lower imputed debt than a fixed capacity type of purchase power agreement such as ADS.

MR. HEMPLING: So the government policy on certainty of recovery is not the sole factor that the rating agencies are taking into account in looking at in determining whether and how much to impute debt?

MR. HERZ: We look at the recovery mechanism and in the calculation of imputed debt where there are wind resources as available and looks at the amount of capacity from that particular agreement would impact the amount of imputed debt.

MR. HEMPLING: Okay. All right. Thank you.

CHAIRMAN CALIBOSO: Any other questions from the staff or commissioners?

All right. This is again Panel 7.

Parties questions of each other, cross-examine, Mr. Williams?

MR. WILLIAMS: No, we do not have any questions.

CHAIRMAN CALIBOSO: Thank you.

MR. WILLIAMS: We just think you did a very thorough job. Thank you.

MR. ITOMURA: The Consumer Advocate has no questions.

MR. MCCORMICK: The Department of Defense has no questions at this time.

CHAIRMAN CALIBOSO: All right.

Let's take a break before our next Panel, 15 minutes, and return at 3:05.

We're in recess.

(Whereupon, at 2:50 p.m., a recess was taken, and the proceedings resumed at 3:06 p.m., this same day.)

CHAIRMAN CALIBOSO: Good afternoon.

We're going to reconvene this hearing with Panel 8.

Maybe starting with witness appearances.

Mr. Kikuta?

MR. KIKUTA: Thank you.

Good afternoon, Chairman Caliboso, Commissioner Cole, Commissioner Kondo, Mr. Hempling.

Peter Kikuta appearing on behalf of Hawaiian Electric. And for Panel 8 we have Lon Okada, Manager of Corporate Taxes for Hawaiian Electric Industries. He is a new panelist; so, he has not yet been sworn in.

CHAIRMAN CALIBOSO: If you could stand, Mr. Okada.

Do you solemnly swear or affirm that the testimony you're about to give will be the truth, the whole truth, and nothing but the truth?

MR. OKADA: I do.

CHAIRMAN CALIBOSO: Thank you. Please be seated.

Mr. Itomura?

MR. ITOMURA: For this panel, the Consumer Advocate has Steve Carver and Mike Brosch. They've been sworn in.

CHAIRMAN CALIBOSO: Thank you.

MR. MCCORMICK: And, surprisedly, the Department of Defense has no witnesses for this particular proceeding.

CHAIRMAN CALIBOSO: Thank you, McCormick.

MR. HEMPLING: Thank you, Mr. Chairman.

Gentlemen, if you would turn to page 75 of the Proposed Settlement Agreement. There's a paragraph 5 on book depreciation, and if you'd also have available the HECO ST-1403 which is a -- it started with Exhibit CA-101, Schedule C-22 page 1 of 1, and superimposed on that CA schedule some information that's blocked out in gray.

My goal is to get an understanding of in 1403, line 3, I'd like to understand the line that's entitled Additional Amortization Net Uncovered where the HECO update number is 1.924 million, the CA adjustment is a negative 1.924 million, and the HECO adjustment is a negative 825,000.

So my question goes to Mr. Carter.

What was the reason for eliminating the 1.924 of additional amortization?

MR. CARVER: In my direct testimony, I discussed this particular item as being a five-year amortization of some stranded costs that the Commission allowed to be amortized in around 2004, and the amortization was scheduled to stop in August of 2009.

The Company, in their forecast, left the full eight months of amortization in the 2009 forecast test year; and, in direct testimony, I removed it on the basis that it would not continue beyond August 2009 since these rates, the rates in which that amortization was embedded would actually continue until the Commission issued the interim order in this case, the Company would have fully recovered those stranded costs from ratepayers; so, that was the original adjustment as opposed to the settlement position.

MR. HEMPLING: And what is your understanding of the reason for the 825,000-dollar adjustment in the next column?

MR. CARVER: For settlement purposes -- well, the Company proposed for settlement that to use a rescheduling of the unamortized amount proposed by the Department of Defense witness and to reschedule it over a two-year period to coincide with the anticipated next HECO rate case.

MR. HEMPLING: So the 825 represents amortization that was supposed to occur in 2009 and you just spread it over two years to make sure it gets recovered before the next rate case?

MR. CARVER: Well, generally, yes, but it's a little more complicated than that, in that the Company's original forecast amortization was understated that they simply got the wrong number in the forecast; so, there was a higher number. I believe it was about 2.1 or $2.2 million that should have been included in the forecast.

So, as part of the correction process, that

2.2 million was being amortized over this rescheduled two-year period, so the 825,000-dollar adjustment has the effect of bringing the Company's original filed amortization of a million 924 down to the million 099 that's in the far, right-hand column of HECO S-1403; so, it's just to get to the right end number.

MR. HEMPLING: Anything to add to this, Mr. Okada?

MR. OKADA: No, I think that was stated quite correctly.

MR. HEMPLING: Thank you.

CHAIRMAN CALIBOSO: Questions anyone? Cross-examine time?

MR. ITOMURA: No questions from the Consumer Advocate.

MR. MCCORMICK: No questions from the DOD.

CHAIRMAN CALIBOSO: Thank you, Mr. McCormick.

At this time, I think we'll just break for the day, because we have scheduled to reconvene tomorrow at 9 a.m. and we will return then and continue with Panel 9 at that time.

So until tomorrow we are in recess.

Thank you.

(Whereupon, at 3:13 p.m., the hearing was adjourned, and is to be resumed on Thursday, October 29, 2009, at 9 a.m.)

CERTIFICATE

This is to certify that the attached proceedings before the Public Utilities Commission of the State of Hawaii In the Matter of the Application of Hawaiian Electric Company, Inc. For Approval of Rate Increases and Revised Rate Schedules and Rules, at 465 South King Street, Honolulu, Hawai'i, commencing, on Wednesday, October 28, 2009, was held according to the record, and that this is the original, complete, and true and accurate transcript that has been compared to the reporting or recording, accomplished at the hearing, that the exhibit files have been checked for completeness and no exhibits received in evidence or in the rejected exhibit files are missing.

Tristan-Joseph, CSR NO. 469, RPR NO. 24906

TRISTAN-JOSEPH, CSR NO. 469, RPR NO. 24906

Hawaiian Electric Company, Inc. • PO Box 2750 • Honolulu, HI 96840-0001

Dean K. Matsuura
Manager
Regulatory Affairs

October 28, 2009

The Honorable Chairman and Members
of the Hawaii Public Utilities Commission
Kekuanaoa Building, First Floor
465 South King Street
Honolulu, Hawaii 96813

Dear Commissioners:

Subject: Docket No. 2008-0083 – Hawaiian Electric 2009 Test Year Rate Case
Hawaiian Electric Hearing Exhibits for Panel 6

Hawaiian Electric Company, Inc. ("Hawaiian Electric" or "Company") hereby submits the enclosed hearing exhibits:

Hearing Exhibit 1 – Year Ahead Sales Forecast Accuracy;
Hearing Exhibit 2 – Sales Forecasts;
Hearing Exhibit 3 – Actual Sales vs. September 2008 Update.

Hawaiian Electric submitted copies of these exhibits to the Division of Consumer Advocacy and the Department of Defense yesterday. Hearing Exhibit 3 contains 2009 sales data that are classified as confidential until Hawaiian Electric Industries, Inc. files its third quarter 2009 financial results with the Securities and Exchange Commission ("SEC") on November 2, 2009. The Company is filing this exhibit subject to the Protective Order filed on November 21, 2008 in this proceeding and will re-file this document on a non-confidential basis following the SEC filing.

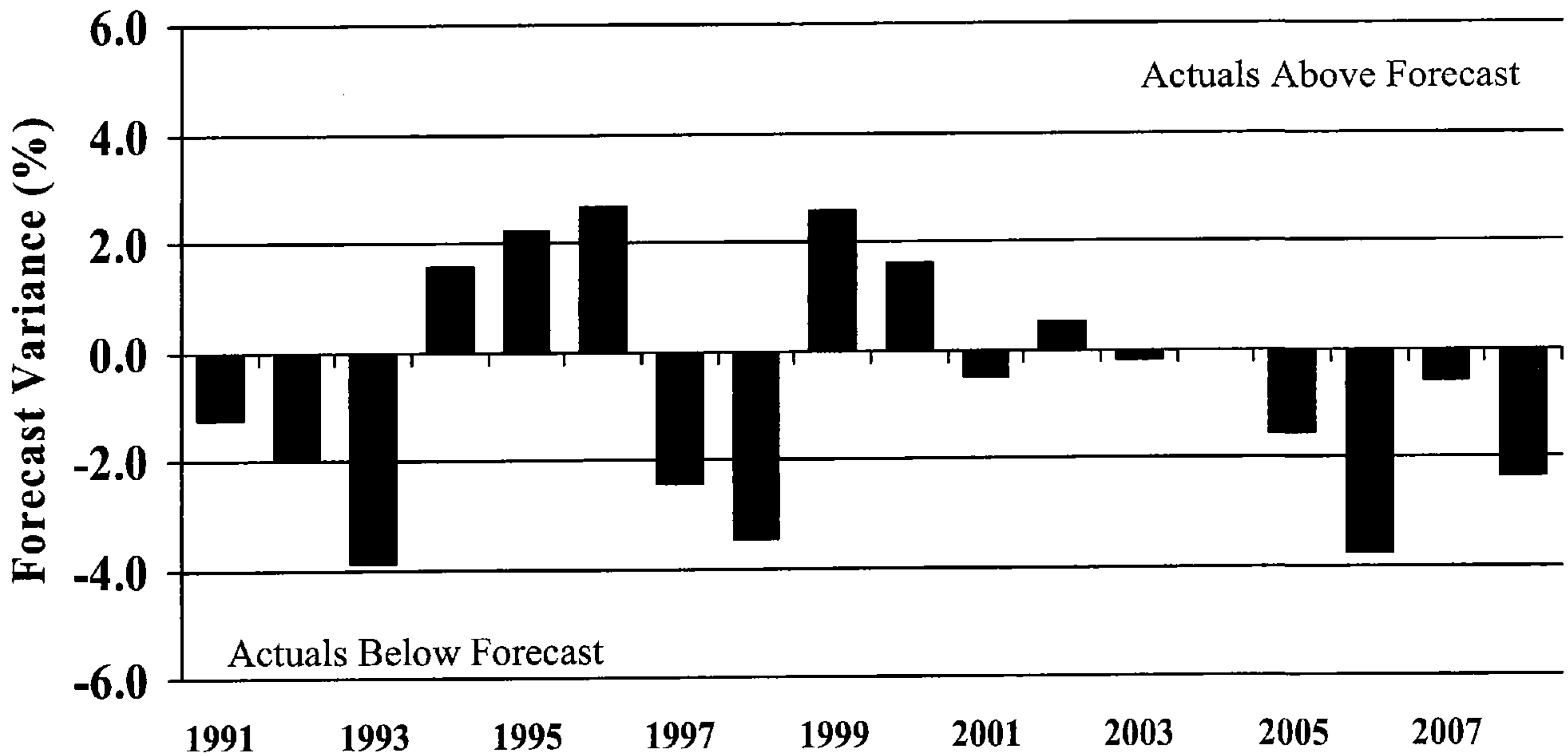
Very truly yours,

Dean K. Matsuura

Enclosures

cc: Division of Consumer Advocacy
Michael L. Brosch, Utilitech, Inc.
Joseph A. Herz, Sawvel & Associates, Inc.
Dr. Kay Davoodi, Department of Defense
James N. McCormick, Department of Defense
Theodore E. Vestal, Department of Defense
Ralph Smith, Larkin & Associates

Year Ahead Sales Forecast Accuracy



Note: Comparisons to non-weather normalized sales. 1991 – 2006 forecasts were developed using CDD weather normalized sales. For 2007-on forecasts, weather was included as an independent variable with forecast values assumed equal to a historical average.

Hawaiian Electric Co., Inc.

YEAR AHEAD FORECAST ACCURACY
GWh Sales

Year	Recorded	Year-Ahead Forecast *	Variance	% Variance
1991	6,539	6,622	-83	-1.25%
1992	6,650	6,787	-137	-2.01%
1993	6,607	6,875	-268	-3.89%
1994	6,797	6,692	105	1.58%
1995	6,963	6,812	151	2.21%
1996	7,091	6,908	183	2.65%
1997	7,040	7,218	-178	-2.46%
1998	6,938	7,188	-250	-3.47%
1999	6,998	6,824	174	2.56%
2000	7,212	7,097	115	1.62%
2001	7,277	7,314	-37	-0.51%
2002	7,390	7,352	38	0.52%
2003	7,522	7,538	-15	-0.20%
2004	7,733	7,735	-2	-0.03%
2005	7,721	7,843	-122	-1.55%
2006	7,701	8,003	-302	-3.78%
2007	7,675	7,721	-45	-0.59%
2008	7,556	7,738	-182	-2.35%

* Forecast prepared in the previous year and used for the budget, for example, the August 2006 forecast for 2007.

HECO HEARING EXHIBIT 2
DOCKET NO. 2008-0083
HECO T-2
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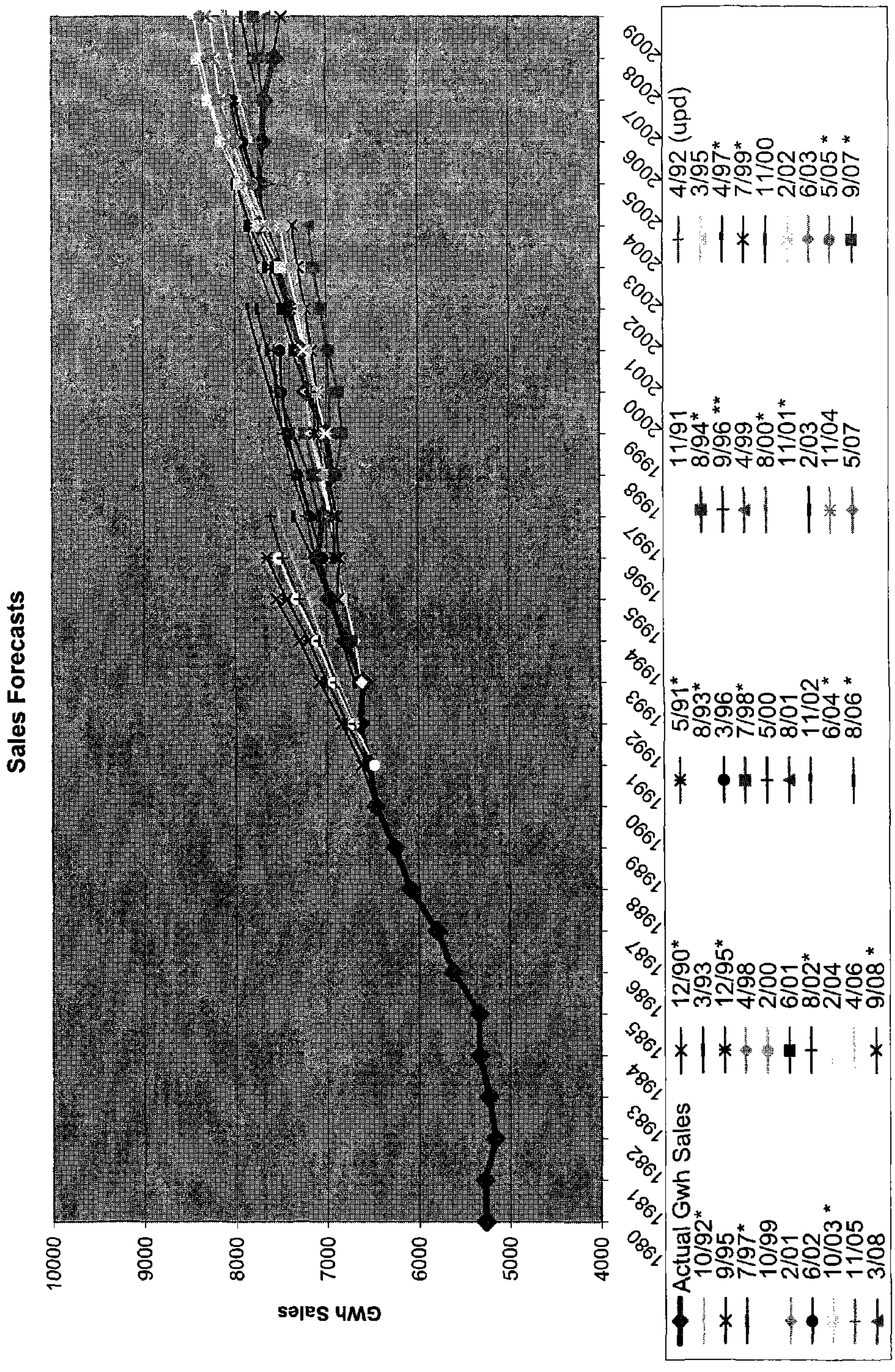

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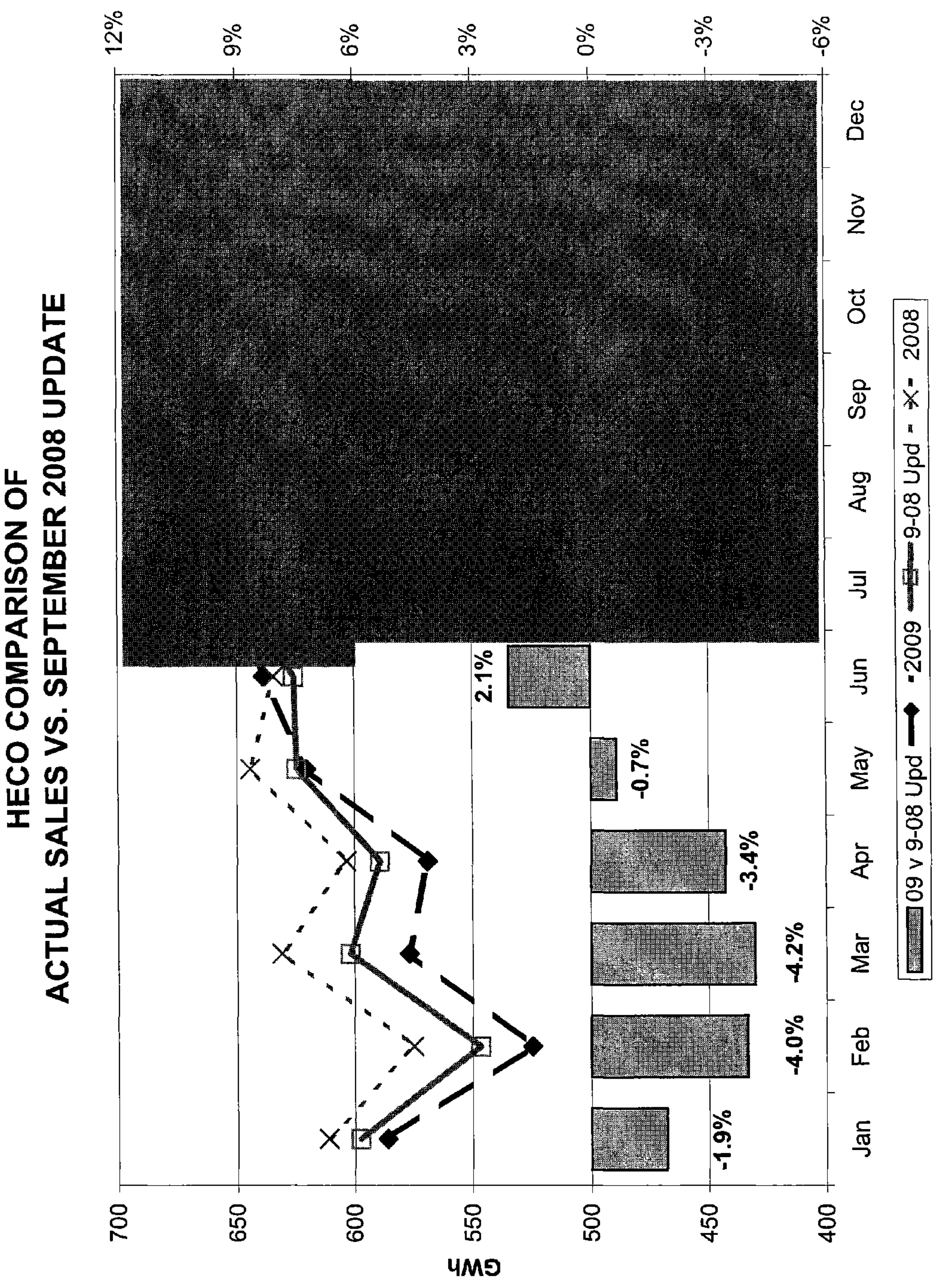
November 21, 2008.



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Hawaiian Electric Company, Inc.
COMPARISON OF RECORDED 2009 VERSUS 2008 AND SEPTEMBER 2008 SALES UPDATE *
September 2009 Year-To-Date

Month	Recorded YTD Sep 2009 GWh Sales	Sep 08 Update * YTD Sep 2009 GWh Sales	Recorded vs. Sep 08 Upd Difference	% Diff
Jan	586.0	597.5	(11.5)	-1.9%
Feb	524.7	546.5	(21.8)	-4.0%
Mar	576.6	601.7	(25.1)	-4.2%
Apr	568.9	589.0	(20.1)	-3.4%
May	620.3	624.4	(4.1)	-0.7%
Jun	638.5	625.6	12.9	2.1%
Jul	[redacted]	650.6	[redacted]	[redacted]
Aug		676.8		
Sep		658.5		
Oct		666.1		
Nov		623.5		
Dec		624.5		
Sep YTD	[redacted]	5,570.6	[redacted]	[redacted]

Month	Recorded YTD Sep 2009 GWh Sales	Recorded YTD Sep 2008 GWh Sales	2009 vs 2008 Difference	% Diff
Jan	586.0	611.0	(25.0)	-4.1%
Feb	524.7	574.8	(50.1)	-8.7%
Mar	576.6	630.8	(54.2)	-8.6%
Apr	568.9	603.5	(34.6)	-5.7%
May	620.3	644.3	(24.0)	-3.7%
Jun	638.5	634.0	4.5	0.7%
Jul	[redacted]	666.3	[redacted]	[redacted]
Aug		669.1		
Sep		646.7		
Oct		653.5		
Nov		612.2		
Dec		609.9		
Sep YTD	[redacted]	5,680.5	[redacted]	[redacted]

* September 2008 Sales Update is the TY 2009 rate case update forecast